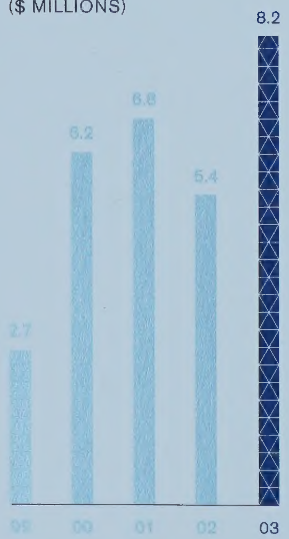
solid principles

MCAP INC. / 2003 ANNUAL REPORT

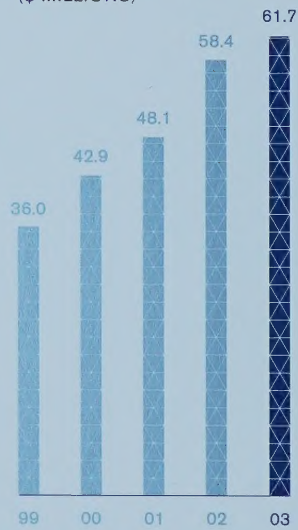
financial highlights

Despite the many challenges encountered in 2003, MCAP grew its business and added another year of strong results to the Company's impressive track record.

NET EARNINGS
($ MILLIONS)

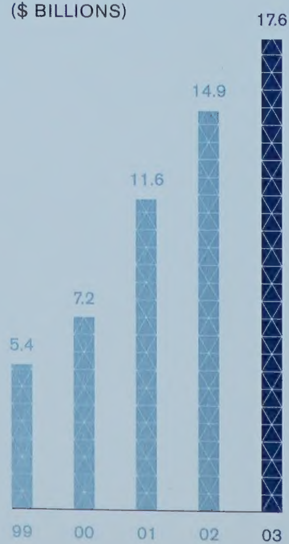


SHAREHOLDERS' EQUITY
($ MILLIONS)

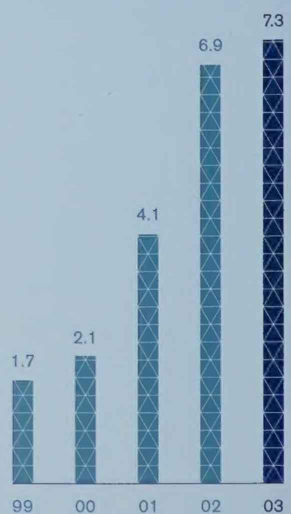


EARNINGS PER SHARE
($)

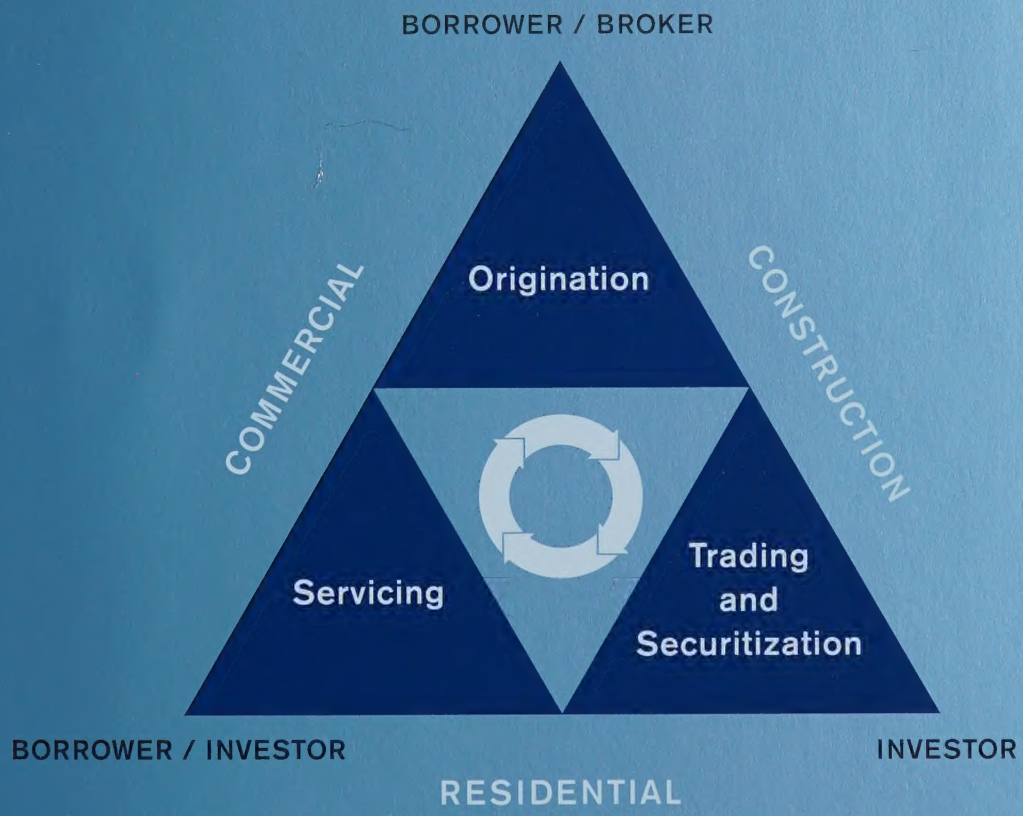
ASSETS UNDER ADMINISTRATION MCAP GROUP
($ BILLIONS)

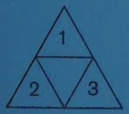


TOTAL MORTGAGE LOANS FUNDED BY MCAP GROUP
($ BILLIONS)



At MCAP, we are committed to excellence in all areas of our business. Through a rigorous discipline of strategic planning, based on solid fundamental principles and values, we have achieved a position of strength in Canada's mortgage and equipment leasing markets.





1_**Origination:** Mainly through brokers, MCAP originates residential and commercial mortgages, construction loans and equipment leases across Canada.

2_**Servicing:** MCAP provides efficient loan/lease administration for its own portfolio, and also derives fee-based revenue from servicing on behalf of other financial institutions.

3_**Trading and Securitization:** MCAP expertly manages its own portfolio, and develops asset management solutions for many investor clients.

achievements in 2003

- During a year of considerable turmoil in financial markets, MCAP grew the Company's assets under administration to more than $17 billion.

- Following the challenges of consolidation in 2002, MCAP recorded earnings of 85¢ per share, aligned with the key goal of producing long-term sustainable earnings for shareholders.

- MCAP focused on operational excellence by implementing new initiatives to improve training, communications and customer service.

- MCAP laid the groundwork for a planned merger of its subsidiary mortgage and leasing operations with CDP Capital – Mortgages, the mortgage operations of the Caisse de dépôt et placement du Québec. The new, merged operations will have a significant market share in Canada, and enable MCAP to significantly increase fees from commercial mortgage operations.

The geodesic dome is a visionary architectural concept. The modular triangles are separate, yet precisely integrated to form an extremely strong, cost-effective structure. Like the geodesic dome, MCAP is based on a visionary concept...one in which each separate business operates independently with its own client base, protecting the clients' individual interests and maintaining confidentiality. Fitted and joined together, the businesses contribute to the overall stability of the whole. Strength is integrated throughout the entire corporate structure, and resides in expert, loyal employees, continuous strategic planning, efficient systems and technology, and effective corporate governance.

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message to shareholders

Stability and strength are recurring themes when we describe MCAP. This year, we chose the geodesic dome as an apt symbol to represent our strong, stable corporate structure. The dome is constructed from separate modules, just as MCAP is composed of a number of separate business units, each of which operates separately and independently, serving its own client group, and protecting client interests and confidentiality.

The businesses join together to form a stable structure. Fitted into the overarching MCAP framework, the businesses are united by a common commitment to effective corporate governance, and continuous strategic planning. They maintain efficient systems and technology, and rally teams of expert, loyal employees.This business model has been effective in helping MCAP achieve success, even during a year of many unprecedented challenges. Throughout 2003, we learned to live with uncertainty. The events surrounding the war in Iraq produced turmoil in financial markets, while the continued fallout from the corporate scandals led to a substantial increase in corporate governance and reporting requirements. As well, the Company faced difficult operational problems due to the SARS emergency and the blackout in Ontario.

Through it all, our employees consistently rose to every unexpected challenge and demonstrated their flexibility and resourcefulness in dealing with change. On behalf of the shareholders, and the senior executive team, I wish to thank our employees for their efforts to ensure the Company's success, and for the many ways they demonstrated their professionalism and commitment to our corporate values.

1_ **Derek Norton,** President and CEO
2_ **Blaine Welch,** Senior Vice-President and Chief Risk and Investment Officer
3_ **Lorne Jenkins,** Vice-President and CFO
4_ **Steven Maker,** President and COO, MCAP Financial Corporation and MCAP Service Corporation and COO, MCAP Mortgage Corporation

Following the challenges of consolidation in 2002, the Company is on track with our goal of steady earnings growth, with earnings per share of $0.85 in 2003. This is an increase over the $0.58 per share achieved in 2002, and all the more significant, given today's low interest rate environment. MCAP has been successful in diversifying income through our leasing business and increasing fee-based revenue through our service business. Mortgage trading, within the well-defined parameters of acceptable risk, has been another profitable area of our business.

In 2003, the Company reached a new milestone of more than $17 billion of assets under administration, up from $15 billion in 2002. MCAP's financial position is strong, with high-quality assets, solid, well-positioned portfolios, and low levels of arrears. The Company is on the path to maintaining long-term sustainable growth, both in earnings per share and assets under administration.

Decisions about the management and future of MCAP have always been determined with reference to our long-term strategic plan. We have consistently followed our principles, and chosen to participate only in those markets where we could effectively compete, and become the customer's first choice for financial solutions. After carefully building the platform for growth, it is gratifying to see our vision beginning to take shape, even in a difficult market.

"We have consistently followed our principles, and chosen to participate only in those markets where we could effectively compete, and become the customer's first choice for financial solutions."

As the next step in our growth strategy, the groundwork has been laid for a merger with CDP Capital – Mortgages, the mortgage operations of the Caisse de dépôt, with the transaction to be completed in the first half of fiscal 2004. Assuming the proposed merger is completed, there will be a change in the Company's structure of ownership. MCAP Financial Corporation and its subsidiary and affiliated operations will be transferred to MCAP Commercial Limited Partnership (MCLP).

According to the terms of the proposed merger, MCAP will have a significant minority interest in MCLP, while CDP Capital – Real Estate Advisory Inc., wholly owned by the Caisse de dépôt, will have a majority ownership share. Notwithstanding a minority interest, MCAP would have access to all of the services and products of the new operations. MCAP would participate in the management and strategic direction of the new operations, and expects that the resulting arrangements will be accretive to earnings. MCAP's existing management team would be responsible for the day-to-day management of the merged operations, and implementing the long-term strategic plan. The Board of Directors of MCAP is in agreement and confident that the proposed merger fits with

our strategic plan to grow the Company, aligned with our key goal of providing long-term sustainable earnings for shareholders. The transaction has been structured to ensure that the individual interests of all our investor and borrower clients are protected, and that their private information is kept confidential. The new, merged operations will remain customer-centric, focusing on customer service and strong relationships.

"The new, merged operations will focus on building volumes in the high value-added areas of the mortgage and equipment leasing businesses, thereby increasing our revenues and profitability."

The advantage of the proposed merger is a more efficient operating structure in the new regulatory environment, and access to, and capital support for, our existing and new funding programs. The transaction will create one of Canada's largest real estate financing operations, with more than $22 billion of assets under management. The new MCLP will thus have greater flexibility to develop more innovative financial products that match the needs of borrowers and investors, differentiated from the standard offerings of the mainstream financial institutions. The new, merged operations will focus on building volumes in the high value-added areas of the mortgage and equipment leasing businesses, thereby increasing our revenues and profitability.

Looking ahead to the challenges of 2004, we do not expect the Canadian economy to grow quickly, and the residential mortgage market is likely to contract. However, MCAP is well positioned to capitalize on further consolidation in the mortgage and banking industry that appears to be on the horizon. Operational excellence gives us an edge. Building on our proven strength as an outsource service provider for our existing financial partners, MCAP can provide cost-competitive services to large financial institutions, and meet or exceed their standards of compliance and reporting.

As you have come to expect from MCAP, we will remain selective and prudent in our investment approach, with the objective of continuing to build long-term sustainable earnings for our shareholders. At the same time, we are ready to press forward and take advantage of the rapid changes occurring in the Canadian mortgage and equipment leasing markets. After the many unexpected challenges of 2003, we are confident that we have an expert team in place, and that team is ready to handle all eventualities.

Derek Norton
President and Chief Executive Officer

1_ **Connie Vann,** Assistant Vice-President – Commercial Real Estate Servicing
Individual managers take ownership of risk management, contributing to effective corporate governance.

2_ **Ken Hughes,** Assistant Vice President – Cash Management
MCAP emphasizes prudent day-to-day management, alongside continuous strategic planning.

3_ **Farah Ahmed,** Mortgage Fulfilment Specialist – Single Family Origination
Efficient systems and technology, and professional service ensure customer satisfaction.

4_ **Marta Pavao,** Receptionist
Expert employees demonstrate their commitment to MCAP's corporate values.

stability

To remain successful, organizations must be able to weather the forces of rapid change. Many factors drive change, including new advances in technology, ever-increasing complexity in financial markets, the pressure for consolidation among financial organizations, and increased requirements for corporate governance and compliance. Within this context of turbulence and change, MCAP maintains stability at the core, deriving its strength from an integrated and dynamic strategic planning process, sound corporate governance, efficient systems and technology, and expert people committed to our corporate values.

Since the Company's inception, MCAP has carefully set down plans for strategic growth, with regular reviews and revisions in light of the changing market and emerging opportunities. MCAP has been successful by focusing on key markets where the Company can achieve its vision of being the customer's first choice for financial solutions. Specialization gives MCAP an advantage, since we can be leading edge innovators in our chosen markets, and respond quickly to changing demands.

"Like the structural supports in a geodesic dome, risk management is integrated throughout the entire organization. Individual managers take ownership of risk management and compliance as a specific accountability for their business."

The Company has benefited from the guidance of a stable and experienced senior leadership team. This team has consistently led the Company on the path to achieve ordered growth, and produce long-term sustainable earnings for shareholders. Furthermore, management's emphasis on operational excellence, and the development of key strategic partnerships has helped the Company earn recognition and respect in financial markets. In 2003, the Company began work on a management succession plan to ensure continued stability in the future.

MCAP demonstrates commitment to the principles of sound corporate governance. In 2001, MCAP implemented an enterprise-wide risk management framework, and in 2002 launched its Legislative Compliance Management System. During 2003, MCAP made progress in developing and solidifying these processes. Like the structural supports in a geodesic dome, risk management is integrated throughout the entire organization. Individual managers take ownership of risk management and compliance as a specific accountability for their business. It is anchored in their commitment to MCAP's corporate values of integrity, pride, responsibility and professionalism.

…wth according …lan

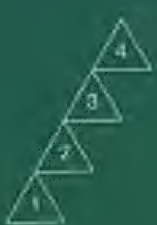
…Company's history, MCAP has made strategic choices … profitability and a pattern of steady growth. … chosen to specialize, and operate only in markets … vision of becoming the customer's first choice … At the same time, MCAP has sought to diversify … reduce reliance on mortgage income. Diversified … and commercial mortgages, construction … leasing have helped to nourish the Company's … structured to provide fully integrated … thereby generating reliable fee-based … partners.

MCAP intends to remain true to this business strategy, and so the proposed merger of its fee-based mortgage and leasing operations in MCAP Financial Corporation with the mortgage operations of CDP Capital – Mortgages is the next logical step in the Company's growth plan. This merger has come about as a direct result of the existing relationship with CDP Capital – Real Estate Advisory Inc. with MFC and MCLP, an alliance of two years' standing. The merger clearly indicates that MCAP has earned a high degree of trust and confidence within the Real Estate Group of the Caisse de dépôt. The merged operations will be responsible for managing the mortgage portfolio of the Caisse de dépôt, and ensuring compliance with all regulatory and legislated standards.

"Diversified revenue streams in residential and commercial mortgages, construction financing and equipment leasing have helped to nourish the Company's growth."

As a result of the merger, there will be a change in the structure of ownership, with the Company taking a significant minority interest in the new operations and CDP Capital – Real Estate Advisory, wholly owned by Caisse de dépôt, taking a majority interest. Although MCAP will have a minority interest, this is outweighed by many advantages. Thanks to the capital support provided by CDP Capital – Real Estate Advisory, the new operations will have more latitude to operate in capital markets, with more opportunities to provide mortgage securitization, and engage in mortgage trading.

The merger is consistent with MCAP's long-term growth strategy. MCAP will be better positioned to increase fee activity and maximize returns on its balance sheet and capital. As for the impact on MCAP's current commercial operations, the merger will propel the Company forward to take a significantly larger share of the commercial market, where the Company can focus on innovative, value-added business activity that will generate increased earnings for shareholders.



1_ **Residential Mortgages:** MCAP ensures customer satisfaction by providing competitive mortgages and efficient service for the life of the mortgage.

2_ **Commercial Mortgages:** The proposed merger with CDP Capital – Mortgages will enable MCAP to provide more innovative solutions for commercial borrowers.

3_ **Construction Financing:** MCAP meets the specialized needs of construction borrowers with flexible funding options and responsive service.

4_ **Commercial Leasing:** Through MTC Leasing, MCAP provides small equipment leasing to businesses.

People Committed to Success:

1_ **Sylvia Pinto,** Executive Assistant – Investment Banking
2_ **Thomas Markandonis,** IT Technical Specialist
3_ **Ian Mucignat,** Senior Manager – Strategic Initiatives, Pipeline Services
Nelson Chu, Manager – Mortgage Trading, Pipeline Services
4_ **Nigel Aplin,** Senior Relationship Manager – Investor Marketing
Sylvia Bessler, Assistant Vice President – Enterprise Risk Management
5_ **Anthony Stilo,** Chief Audit Officer
6_ **Lorraine MacFarlane,** Administrative Assistant – Human Resources

individual and collective strength

2003 was a pivotal year in developing our people to support operational excellence. MCAP continued to invest in training for employees at all levels of the organization, in areas such as technology, customer service skills and product knowledge. To help ensure the Company's management team is strong, MCAP provides an in-house Management Development Program, now in its fourth year, as well as an intensive learning path for senior leaders involving 360-degree feedback, personal development, and individual coaching.

In 2003, MCAP enhanced its performance management system to ensure that all employees are compensated, rewarded and recognized for the many ways in which they support the Company's values; namely: Pride, Integrity, Responsibility, Innovation, Professionalism, Teamwork Commitment, and Fun. The "Award of Excellence" in-house recognition program encompasses all employees, and is designed to recognize outstanding performance. All contributions are valued, including innovations that improve business efficiency, stellar achievements in sales and customer service, and initiatives that help build team spirit within the Company.

"The Company was proud to achieve the ranking of 53rd on the Best Employers in Canada Survey."

Demonstrating their community involvement, MCAP's employees again supported the United Way campaign, and MCAP matched employee donations with corporate giving. Moreover, employees broke previous fundraising records for Habitat for Humanity, an organization that helps low-income families realize their dreams of home ownership.

MCAP is committed to the strategic objective of becoming an Employer of Choice. In support of that objective, and to obtain feedback directly from our employees, MCAP participated in an independent, enterprise-wide employee survey administered by Hewitt Associates, and sponsored by the Globe and Mail Report on Business. The Company was proud to achieve the ranking of 53 out of 125 Best Employers in Canada. The results of the survey indicated that our employees are fully engaged, confident in the leadership of the Company, and supportive of MCAP's vision, business strategy, and values.

Moving forward, MCAP will continue to invest in training and developing our employees, and to enhance our people management practice, so that we maintain a strong team of expert, loyal employees.

Management's discussion and analysis of operations

This Management's Discussion and Analysis of Operations (MD&A) should be read in conjunction with the Company's Consolidated Financial Statements for the year ended December 31, 2003 and related notes thereto. This MD&A has been prepared as at March 16, 2004.

This MD&A has been prepared by reference to the new MD&A disclosure requirements established under proposed National Instrument 51-102 "Continuous Disclosure Obligations", ("NI 51-102") of the Canadian Securities Administrators. While NI 51-102 is not expected to be proclaimed in force until March 30, 2004 management believes that utilizing NI 51-102 as a guideline for enhanced disclosure will provide greater insight into, and understanding of, the Company's financial condition and operating results.

Additional information regarding the Company, including copies of the Company's continuous disclosure materials such as the Corporation's annual information form, is available on the Company's website at www.mcap.com or through the SEDAR website at www.sedar.com.

In 2003, MCAP Inc. (the "Company" or "MCAP") enjoyed a profitable year from its core business lines and completed activities that strengthened the Company's foundation to generate long-term sustainable earnings. MCAP is Canada's largest independent mortgage Company, participating in all aspects of the Canadian mortgage market with origination, underwriting, funding and servicing capabilities in all of its core business lines. The Company, through its subsidiary MTC Leasing Inc. (MTCL), is also a significant originator and administrator in small equipment leasing.

During 2003, MCAP developed new securitization programs that will provide the Company with funding sources to originate mortgages through its existing broker network. In the fourth quarter of 2003, the Company, in partnership with CDP Capital – Real Estate Advisory Inc., launched the first residential construction mortgage securitization program in North America. This program is complementary to existing funding sources and provides a predictable funding source that allows the Company to fund construction loans in all sectors of the residential construction market. The Company also developed a commercial term mortgage securitization program and a sub-prime single-family residential mortgage securitization program. These are expected to be launched and operational in the first half of 2004.

The Company began to benefit from expanded access to borrowers through Canada ICI Commercial Mortgages Inc. (Canada ICI) as new structured finance programs were launched. These new programs will allow the origination and administered asset volumes to grow in the commercial and construction business lines.

The Company combined the funding and administrative servicing activities of the residential construction and commercial mortgage operations of MCAP Commercial Limited Partnership (MCLP). This change positions the Company

A Note About Forward-Looking Statements

This annual report contains forward-looking statements about MCAP. A forward-looking statement is subject to risks and uncertainties that may be general or specific. A variety of factors, many of which are beyond MCAP's control, affect the operations, performance and results of MCAP, and could cause actual results to differ materially from the expectations expressed in any of MCAP's forward-looking statements. These factors include current, pending and proposed legislative or regulatory developments; intensifying competition, resulting from established competitors and new entrants in the financial services industry; technological change; capital market activity, including interest rate fluctuation and general economic conditions; changes in market rates and prices which may adversely affect the value of financial products; and MCAP's success in managing the costs associated with the expansion of existing distribution channels, developing new ones and realizing increased revenue from these channels. This list is not exhaustive of the factors that may affect any of MCAP's forward-looking statements. These and other factors should be considered carefully and readers should not place undue reliance on MCAP's forward-looking statements. MCAP does not undertake to update any forward-looking statement that is contained in this annual report.

to improve service levels for borrowers and investors, to leverage complementary technologies, and to increase operational efficiencies relating to administration and reporting functions.

The Company's operations delivered some significant achievements in 2003.

Operational Highlights:

- Assets under administration for MCAP and affiliated companies exceeded $17 billion.
- Consolidated assets exceeded $ 369 million.
- Recorded earnings per share of $0.85, versus $0.58 per share in 2002, an increase of 46.6 percent.
- Eleven consecutive years of positive quarterly and annual earnings.
- Launched the first residential construction mortgage securitization program in North America.
- Launched a Home Equity Line of Credit (HELOC) for both insured and conventional borrowers.
- Developed a securitization structure for commercial term mortgages and for residential sub-prime mortgages expected to be launched in the first half of 2004.
- Residential construction mortgages under administration exceeded $1 billion.
- Combined the commercial servicing and residential construction mortgage group.
- Added a Standard & Poor's rating as master and special servicer for commercial mortgages to the primary servicer rating achieved in 2002.
- Rated 53rd out of 125 Best Employers in Canada, according to an independent survey administered by Hewitt Associates, and sponsored by the Globe and Mail Report on Business.
- MCAP Inc. and CDP Capital – Real Estate Advisory Inc. announced an agreement in principal for the merger of the mortgage operations of MCAP with CDP Capital – Mortgages.

Vision, Mission and Corporate Values

MCAP's vision and mission have been determined through the Company's strategic planning process and provide the direction for the Company's ongoing activities. The Company's stated vision is, "To be the first choice for financial solutions in our chosen markets." The Company's mission is, "To originate, underwrite and service mortgage and leasing assets that best serve the needs of our borrowers and investors." MCAP's employees are key to making the vision and the mission a reality. Employees demonstrate the Company's corporate values in the way they conduct business activities, and interact with investors, customers and each other. These values, namely: Pride, Integrity, Responsibility, Innovation, Professionalism, Teamwork Commitment, Fun and Respect ensure the Company's work environment is based on professionalism and mutual respect. By upholding these values, MCAP has created a workplace where the top performers in the industry want to work.

Operational Business Segments

MCAP operates in three key business segments: Investing Operations, Mortgage Operations and Leasing Operations.

Operations – Income Sources

Investing Operations	Mortgage Operations	Leasing Operations
Activities	Activities	Activities
• Asset & Liability Management	• Origination	• Origination
– Mortgages	• Underwriting	• Underwriting
– Leases	• Funding	• Funding
– Marketable Securities	• Servicing	• Servicing
– Cash	• Mortgage Trading	• Securitization
– Debentures	• Asset Warehousing and Aggregation	
• Credit Management	• Securitization	

Investing Operations

The Company's investing operations include asset and liability management, which utilizes the capital and leverage capabilities of MCAP Inc. These investing activities are managed by the risk management function, which oversees all risk decisions in all investing, operational and investment banking initiatives, including MCAP's financing and asset acquisition activities. The Company is a federally regulated loan Company. As a result, MCAP can issue Canada Deposit Insurance Corporation (CDIC) insured deposits and invest these funds to earn spread income. The Company invests its capital and debt in cash and cash equivalents, single-family residential mortgages, variable rate residential construction mortgages, commercial term mortgages, marketable securities and other assets. The Company's investment limits are determined by its regulated limits and by its own investment policies as approved annually by the Board of Directors. The investing operations are complementary to the mortgage and leasing operations. The Company, through its subsidiary operations, is able to originate, fund and aggregate mortgages and leases for the purpose of resale or securitization. The mortgage and leasing operations provide a wide range of assets for the Company's investing operations. The Company may choose to sell some of these mortgages from time to time for capital management purposes, or to take advantage of market opportunities. In turn, the Company's funding capabilities provide the mortgage and leasing operations with diversified, predictable funding sources and the ability to earn income from mortgage trading activities.

Mortgage Operations

The mortgage operations generate fee income from the origination, underwriting, funding and servicing of single-family residential mortgages, residential construction mortgages and commercial mortgages. The mortgage operations earn investment income from aggregating mortgages and then selling these mortgages to third-party investors or to securitization trusts. The single-family residential operations are conducted primarily through our 20 percent owned affiliate, MCAP Service Corporation (MSC). The Company's non-traditional single-family residential mortgage operations, including the sub-prime and covenant recovery businesses, are conducted in MCAP Financial Corporation (MFC). The sub-prime single-family residential mortgage business is a high-yield security-based lending program, in which the underlying real estate is the primary determinant in credit adjudication. MCAP can generate attractive yields through this sub-prime business, given that the Company can effectively manage the higher risk of arrears through proactive collection and recovery activities. The covenant recovery business involves recovering amounts previously written off by our third-party investors, and sharing in a portion of these recoveries. Residential construction lending and servicing, and commercial mortgage origination and servicing are conducted in MCAP Commercial Limited Partnership (MCLP) and Canada ICI Commercial Mortgages Inc.

Leasing Operations

The Company's leasing operations are conducted through our wholly-owned subsidiary MTC Leasing Inc. (MTCL). With a client base across Canada, MTCL originates, underwrites, funds, services and securitizes small equipment leases. The leasing Company generates new business through direct vendor relationships and through lease brokers. This is a competitive business with high volumes of transactions, so MTCL has made considerable investments in information technology in order to streamline operating procedures. MTCL has developed industry-leading, state-of-the-art lease application processing systems, as well as an automated credit adjudication system to support the sales staff. The lease administration system is capable of handling very large volumes of transactions, while providing effective reporting to management and the investor/borrower customers. Therefore, MTCL has been developing new business leads to sell outsourcing services to other leasing companies, in order to broaden MTCL's servicing income sources and to grow its portfolio of leases under administration. MCAP believes that the leasing operations can capitalize on opportunities by focusing on areas of the market that are currently under-serviced, and providing outsource solutions.

Business Developments

In 2003, the Company completed and brought to market one of the most innovative securitization structures in the country. Together with its partner, CDP Capital – Real Estate Advisory Inc., MCAP launched the first residential construction mortgage securitization program in North America. The program is a revolving finance structure that provides ongoing funding for variable rate residential land development loans and residential construction mortgages. This program is evidence of the Company's ability to differentiate MCAP from the competition by providing innovative, niche financial product offerings. This program adds much needed capacity to this line of business.

The Company has expanded its residential lending opportunities by entering the sub-prime single-family mortgage market. This business line focuses on originating higher yielding mortgages, in which the underlying security (real property) is the leading determinant for credit approval. This deviates from traditional mortgage lending in that the borrower's credit record and proof of income are not the primary criteria for adjudication. Compared with traditional lending, the sub-prime mortgage product provides new home ownership opportunities to a wider consumer base. Given that MCAP is committed to prudent selection of high quality real properties, careful management of arrears, and effective collection activities, the Company believes the higher yield on these mortgages more than offsets the higher risk. In addition, the Company has developed a securitization program designed to fund these mortgages and yield an attractive interest spread for the Company. This program is scheduled to come to market in the first half of 2004.

The Company has developed a commercial term mortgage securitization program that was launched in the first quarter of 2004. This program provides an additional funding source that enables the Company to expand its origination and servicing revenues in this business line. In 2002, Standard & Poor's provided the Company with a rating as a primary servicer of commercial mortgages. In 2003, the Company attained the additional ratings of master and special servicer of commercial mortgages. These ratings help to differentiate the Company from the competition in this market. With the regulatory rules governing the servicing of securitized assets expected to change in 2004, the Company has positioned itself to take immediate advantage of opportunities that arise.

MCAP makes considerable investments to maintain high standards in business processes, technology and corporate governance. The Company's clients are highly regulated institutions, so it is imperative that our business practices meet or exceed the scrutiny of all regulators. Commitment to operational excellence is a unique differentiating factor that sets the MCAP group of companies apart from other mortgage and leasing service providers. Investing in operational excellence is a successful strategy. This is apparent from the Company's significant growth in administered assets, as well as its ability to obtain third-party servicer ratings in multiple lines of business. Furthermore, the Company conducts annual surveys of its investor clients, and the feedback indicates that clients clearly value MCAP's strong business controls and high standards of service.

In the fourth quarter of 2003, MCAP Inc. and CDP Capital – Real Estate Advisory Inc. announced an agreement in principle for the merger of the mortgage operations of MFC and its subsidiary and joint venture operations in MCLP with CDP Capital – Mortgages. Currently, CDP Capital – Real Estate Advisory Inc., through a subsidiary Cadcap Inc., has a 50 percent interest in MCLP, and through other holdings has a significant interest in MFC through a subordinated convertible debenture. Under the terms of the new proposed structure, CDP Capital – Real Estate Advisory Inc. will hold a majority interest in the combined operations, while MCAP will hold a significant minority interest. MCAP will be involved in the strategic direction of this merged operation, and will continue to benefit from the services it provides.

The Company is moving from a majority position in the existing MFC businesses to a minority position in the combined, but significantly larger group. The structure provides for a more appropriate regulatory framework for our businesses and eliminates areas of conflicting regulations and overlapping oversight. The businesses that will be combined are complementary, and the Company expects to benefit from the larger lending base and innovative financial structures that this business can bring to the Canadian market. There were no agreements signed or executed at the date of release of this MD&A.

SUMMARY OF FOURTH QUARTER ACTIVITIES

In addition to the fourth quarter activity described under the Business Developments section of this MD&A, the Company reported net income for the quarter ended December 31, 2003 of $2.3 million or $0.24 per share, compared to $2.0 million or $0.21 per share last year. The annualized pre-tax return on average equity based on quarterly earnings was 15.3% up from 13.4% for the same period last year. Earnings in the quarter were consistent with the trends established during the previous three quarters.

Net investment income, reflecting net earnings on invested assets, was $4.2 million compared to $5.2 million earned in the same period of 2002. Net mortgage interest income was $1.6 million in the quarter consistent with the prior year. The average mortgage balance increased from $225 million in the fourth quarter of 2002 to $255 million in the current quarter. Matched mortgage spreads were 2.62% at December 31, 2003, compared to 2.39% at December 31, 2002. Matched spreads including mortgages and cash were 2.44% at December 31, 2003 versus 2.53% at December 31, 2002. This is a result of an increase in cash balances from $9.4 million at December 31, 2002 to $31.4 million at December 31, 2003.

Gains on sales of mortgages for the quarter were $118,000 compared to $1.5 million last year. The Company reduced its mortgage trading activity in the quarter due to lower profit margins available in the market. During the period, the marketable securities portfolio generated an annualized return of 21.0% contributing $477,000 including realized gains of $277,000. During the fourth quarter of 2002, the marketable securities portfolio generated an annualized return of 19.55% contributing $757,000 to income. The average marketable securities portfolio during the fourth quarter of 2003 was $6.4 million lower than the fourth quarter of 2002. Leasing income of $1.7 million was $266,000 lower than last year.

The Company's mortgage and leasing operations generated total fees of $5.8 million, which was $525,000 higher than the prior year. The Company's share of total fees, net of interest and other costs associated with the financing last year, increased from $2.6 million to $3.5 million.

Operating expenses during the quarter were $5.4 million or $525,000 lower the same period last year. Operating expenses in the quarter were 69.6% of Revenue from operations compared to 75.1% in 2002. Lower salaries, incentive compensation and occupancy costs contributed to this favourable result.

The following section will detail the Company's annual operating results by key business segment.

FROM OPERATIONS

Earnings for the year ended December 31, 2003, were $8.2 million, up $2.8 million from 2002. Earnings per share were $0.85 versus $0.58 per share in 2002, an increase of 46.6 percent. The pre-tax return on average equity was 14.0 percent versus 10.8 percent in the previous year. During the year, shareholders' equity increased from $58.4 million to $61.7 million, as earnings exceeded dividends and the Company issued shares from treasury to satisfy the dividend reinvestment plan.

The Company's core operations continued to deliver steady consolidated profitability and the activities of 2003 supported and enhanced the potential for long-term sustainable earnings. The Company's net income from investing operations increased by 86.2 percent, as the capital raised in 2002 was optimally deployed for a full year in 2003. The leasing operations had another successful year with net income of $1.6 million compared to $1.5 million in 2002, despite slower spending by enterprises on plant and equipment in 2003. An abundance of investor capital funding for both commercial and construction mortgages led to competitive market pressure. This hindered the Company's commercial and construction mortgage operations by reducing the total spread and fees available on each transaction, and, in part, reduced earnings, resulting in a loss of $263,000 in the current year, compared to income of $234,000 in the prior year. The Company's 2003 activities included developing unique structured finance programs and making considerable effort to improve operational efficiency and to reduce costs. Consequently, the mortgage operations are well positioned with efficient operations and excellent funding capabilities to grow profitability in 2004.

Net Investment Income

Consolidated net investment income was $18.3 million for the year, compared to $15.5 million in 2002. Net investment income represents earnings from balance sheet investment activities, net of interest expenses, provision for losses and other related costs.

Investing Operations

Investment income earned from net interest spread increased from $6.1 million in 2002 to $8.4 million in 2003. The Company raised capital in February of 2002 and deployed this capital throughout the year. As a result, 2003 saw a full year of earnings from this higher capital. The Company repositioned its asset mix to hold a greater portion of high-yield residential construction mortgages and sub-prime residential mortgages. The Company's average cost of borrowing declined from 4.0 percent in 2002 to 3.6 percent in 2003, as the debenture portfolio repriced at lower market rates. The Company's floating rate mortgage investments were funded in part by fixed rate debentures, and as a result there is a delay between the repricing of the mortgage assets and the repricing of the debentures. Average mortgage balances increased to $260 million in 2003 from $197 million in 2002. The Company maintained an average yield on the mortgage portfolio of 6.6 percent, which was consistent with the prior year, even as mortgage rates fell during the year. Repositioning the balance sheet allowed the Company to earn gains from the sale of older, higher yielding mortgage investments while still maintaining the yield on the Company's overall portfolio.

Marketable securities income of $2.4 million declined from $3.0 million in 2002, but continued to perform well with an annual return on investment of 18.7 percent. The marketable securities portfolio ended the year with unrealized gains of $1.3 million, compared to $758,000 at the end of 2002.

There was an overall decrease in the allowance for loan losses of $584,000 relating to the mortgage portfolio, compared with an increase of $519,000 in 2002. Of the total change, $509,000 related to a decrease in the specific allowance, primarily related to the workout of one residential construction loan, with the balance of $75,000 related to a reduction in the general allowance for loan losses. The general allowance represents at least 1.0 percent of risk-weighted assets, consistent with the previous year. The general allowance moderately declined, since the mortgage portfolio was $241 million at year-end, compared to $251 million the year before. The Company continued to experience low levels of write-offs, averaging 6.6 basis points on average mortgage balances, compared to 8.1 basis points in the prior year.

In 2003, arrears levels were 4.03 percent, up from 2.72 percent in 2002. Higher arrears at year-end were related to a larger holding of sub-prime mortgages than was the case in 2002. Net impaired loans ended the year at 0.55 percent of the total mortgage portfolio, down from 0.89 percent in 2002. MCAP continues to proactively monitor mortgage arrears, and to take prudent steps to collect overdue accounts. Provided that real estate markets remain stable, management does not expect an increase in loan loss experience in 2004.

Mortgage Operations

The Company's mortgage operations contributed $4.2 million to net investment income, compared to $4.0 million for 2002. The Company achieved another profitable year from its mortgage trading activities. MCAP, through its subsidiary operation in MFC, acts as a mortgage aggregator for certain third-party investors and also sells a portion of its own mortgage investments from time to time as part of its capital management practice, or to take advantage of favourable market opportunities. The Company earned $2.4 million in gains from mortgage trading activities, compared to $2.3 million in 2002. The majority of these gains were earned from the sale of a portion of the Company's mature, higher yielding portfolio of mortgages. These assets were attractive in the market due to the continued low interest rate environment and the underlying credit quality of the mortgages. The Company's capacity to originate residential construction mortgages and sub-prime residential mortgages increased in 2003. As a result, the Company was able to sell the older mortgages in the portfolio at a profit, and replace them with assets that provide a similar yield.

Equity income from partly-owned companies, representing the Company's 20 percent share of MSC and MCAP Mortgage Corporation (MMC), was $817,000, compared to $961,000 in 2002. These affiliated companies represent the majority of the Company's interest in the single-family residential mortgage operations. The decline in results is due to lower origination volumes in the first quarter, when these companies introduced the new Mercury™ mortgage origination and underwriting system. By the end of the year, volumes had returned to normal levels, with operations committing $5.8 billion in new mortgages. Total mortgages administered were $12.9 billion at year-end, compared to $10.5 billion recorded in the previous year.

The Company earns net interest income in connection with its mortgages under administration. This revenue relates to interest earned on escrowed balances held to pay property taxes or required as cash collateral in support of the various residential construction loans. In 2003, the larger portfolio of administered mortgages resulted in higher net interest income of $982,000, compared to $714,000 in 2002.

Leasing Operations

Net investment income earned from the Company's leasing operations was $4.8 million, increasing from $4.7 million a year earlier. The Company earns investment income from leases held for its own account, from leases held for resale, and from gains recorded on the sale of leases to third-party investors and securitization trusts. This investment income is reduced by the cost of borrowing to fund the leases and from credit provisions. Total new lease production of $42 million was marginally behind last year's production of $45 million. Total leases under administration were $77.8 million, compared to $74.6 million in 2002. MTCL has the capabilities to produce higher volumes of new business; however, lower spending on plant and equipment by commercial enterprises led to reduced total volumes for 2003. MTCL is seeking to expand opportunities in the medical and dental equipment field and is considering other initiatives in the mid-size equipment leasing market. Management continues to explore new opportunities to grow this business.

The allowance for specific losses from leases decreased by $646,000 in 2003, compared with an increase of $232,000 in 2002. The allowance was increased by $868,000 as a result of the growth in the total lease portfolio in 2003, compared to an increase of $1.3 million in 2002. Accounts determined to be uncollectible and written off in 2003 were $1.5 million, compared to $1.0 million in 2002. These write-offs resulted in a decrease in the net non-performing portfolio, from 0.52 percent of the total portfolio in 2002, to 0.38 percent in 2003. Arrears (defined as accounts outstanding over 30 days) increased slightly to 0.82 percent at the end of 2003, from 0.64 percent at the end of 2002.

Fee Income

Consolidated fee income derived from Company operations was $13.8 million, an increase of 2.8 percent from $13.5 million a year earlier. Fee income is directly related to the Company's mortgage and lease assets under administration. Total assets under administration, including equity accounted affiliated operations, are as follows:

Assets under Administration (000's)

	2003	2002
Single-family residential mortgages	**$ 12,912**	$ 10,507
Commercial mortgages	**3,469**	3,386
Residential construction mortgages	**1,057**	894
Equipment leases	**78**	75
Other	**86**	79
	$ 17,602	$ 14,941

Investing Operations

The Company earns mortgage fees on its own portfolio of mortgages. During 2003, the average mortgage portfolio balance was $260 million; this was $63 million higher than in 2002. As a result, the Company's fee income, including commitment fees and borrower paid fees (such as renewal, discharge, extension), was $1.2 million. This compares favourably to $740,000 of fee income generated from a smaller portfolio in 2002.

Mortgage Operations

The majority of the Company's fee income arises from the mortgage operations. Fee income is highly dependent on new mortgage origination and servicing activities in MCLP. All fees derived from the MCLP operations are shared with CDP Capital – Real Estate Advisory Inc.

A small portion of fee income arises out of mortgage origination and servicing of residential mortgages, and other administrative services provided in MFC. All fees generated by MFC are retained 100 percent by the Company.

The more MCLP generates in new mortgage volumes and the larger the mortgage assets administered, the higher the total fees will be. The Company does not earn fee income directly off the $12.9 billion portfolio in MSC; instead, MCAP shares in 20 percent of the after-tax profit of MSC, which is reported in the Company's net investment income line. The total fees generated by the mortgage operations were $17.1 million compared to $17.5 million a year earlier. The Company's share of total fees was $8.5 million versus $9.6 million in 2002. The difference in total fees generated is attributed to two factors. In 2003, MCLP shared a higher proportion of fees with third-party investors, and for the first two months of 2002 the Company retained 100 percent of its broker origination fees earned in MFC.

During 2003, the Company generated $5.5 million of commercial mortgage origination fees, net of commissions, which exceeded the $4.8 million earned in 2002. The Company's share of these fees was $2.8 million, versus $2.4 million a year earlier. The total new business volume originated exceeded $2.2 billion.

The Company's residential construction lending activity originated $885 million in new business in 2003, up from $771 million in 2002. Net commitment fees earned were $2.0 million compared to $2.5 million last year. The Company's share of these fees was $1.0 million compared to $1.4 million in 2002. In 2003, MCLP shared a greater proportion of net commitment fees with its investor client base, and as a result there were lower fees to be shared between the joint venture partners.

Servicing and other fees earned from the portfolio of administered mortgages were $9.6 million compared to $9.9 million in 2002. The Company's share of these fees was $4.8 million compared to $5.7 million in 2002. However, during 2002, the Company retained 100 percent of the servicing fees of $1.5 million, up until the joint venture was reorganized, effective March 1, 2002.

During 2003, the Company combined the residential construction operation with the commercial servicing operation, in order to improve operational effectiveness and to reduce costs. Commercial origination activity is carried out by Canada ICI Commercial Mortgages Inc., and it continues to operate independently within the MCAP group of companies.

MFC's administrative and servicing fees from its non-traditional single-family operations, including sub-prime, contributed total fees of $4.1 million compared to $2.8 million a year earlier. During the year, the Company generated $75 million in sub-prime loans and MCAP retained $54 million for its own investment purposes. The addition of the sub-prime mortgage business, combined with higher administrative fees, accounted for the increase year over year.

Leasing Operations

The Company's leasing operations generated fees of $2.0 million in 2003, an increase of $140,000 over fees of $1.9 million earned in 2002. The recovery in Canadian commercial spending on machinery and equipment was more moderate than expected. The Company's leasing operations also demonstrated a similar pattern with moderate growth through the year. Early indicators in 2004 are showing an improvement to commercial spending on plant and equipment, which is a positive indicator for the leasing business. The current operations can manage significant growth of business volumes within the existing infrastructure. The implementation of a new front-end system, Express OS™, allows the Company to provide an even higher level of customer service and creates further capacity to handle the expected increase in volumes in the future. The Company believes the leasing business is very well positioned to seize opportunities and grow revenues in this consolidating but vibrant industry.

Operating Expenses

Consolidated operating expenses increased by $170,000 to $21.2 million in 2003. Expenses as a percentage of revenue from operations were 71.7 percent, down from 78.6 percent in 2002. The Company's investments in technology and operational excellence have enabled an increase in business volumes and revenues with a much lower relative increase in costs. The number of employees in the Company's subsidiary and joint venture operations declined from 216 in 2002, to 209 employees in 2003, primarily due to efficiencies introduced in the commercial and residential construction mortgage business. Salary costs declined by $714,000, but these savings were offset by increased costs related to information technology, professional fees, capital taxes and other administration costs. Overall, the number of employees for the MCAP group including affiliates increased marginally from 552 in 2002, to 560 in 2003. As stated earlier, the Company is committed to differentiating itself from the competition by investing in its people, technology and corporate governance. During 2003, many of the technological solutions developed as a result of the Company's significant information technology investments were leveraged across multiple business lines.

During 2002, the Company introduced two significant technology solutions to the business. The single-family residential operation launched the Mercury™ mortgage front-end system that links new mortgage applications to the back-end administration system. The leasing operations launched a new front-end system Express OS™ that introduced an online application processing, credit adjudication and a link through to the lease administration system ASSET™. During 2003, the Company focused on achieving increased customer service and operational efficiencies anticipated from the new technologies. The Company introduced changes to processes and workflows to benefit fully from these new systems.

Operational excellence is critical to the Company's business success. There are many definitions of operational excellence, since it is a practice or philosophy that is defined differently in every organization. At MCAP, operational excellence occurs when employees work both individually and collectively, in an effective and efficient manner, to achieve the goals set out in the Company's strategic plan, while demonstrating MCAP's corporate values. The Company utilizes a performance management system designed to promote and reward operational excellence. Every year, employees work to achieve new targets that are aligned with the Company's strategic plan. Employees are evaluated and rewarded based on how well they achieved their targets and demonstrated the corporate values. Annual incentives are heavily weighted to reward top performance and achievements that contribute to operational excellence.

The selected financial information provided on pages 51–53 of this Annual Report summarizes certain selected consolidated financial information of the Company for the last three completed fiscal years and the last eight completed quarters. This financial information has been prepared on a basis that is consistent with the Canadian generally accepted accounting principles applied to the annual financial statements.

The Company has experienced growth in its net investment income over the last three years. This growth resulted from increases in invested assets and changes to the mix of those assets as the Company's capital has grown. While the yield on average assets declined in 2002 and 2003 as the prime rate declined, the Company continued to achieve strong gains from the marketable securities portfolio and mortgage trading activity.

Consolidated fee income recognized by the Company has remained flat over the previous three years as the Company reorganized its mortgage operations. The acquisition of MTCL in 2001 and the Canada ICI Mortgage group in 2002 have contributed to the growth in total fee revenue; however, the Company shared a larger percentage of these fees with its investors and joint venture partners. Total fee income has grown from $15.2 million in 2000 to $23.2 million at the end of 2003. The Company's share of these fees was $13.8 million at December 31, 2003.

Operating costs have increased due to the growth in volumes. Expenses as a percentage of revenue from operations were 71.7 percent in 2003 compared to 78.6 percent in 2002 and 74.6 percent in 2001. The Company's investment in technology and operational excellence have allowed for an increase in volumes and revenues with a much lower relative increase in costs. Total employees of MCAP including affiliates have risen from 552 in 2002 to 560 in 2003. The number of employees in the Company's subsidiary and joint venture operations declined from 216 in 2002 to 209 employees in 2003 primarily due to efficiencies in the commercial and residential construction mortgage business. The Company only consolidates 50% of the operating expenses of MCLP.

Net income has been relatively stable over three years with the exception of a decline in the second quarter of 2002. This decline was due primarily to acquisition integration costs, compression of net interest spread on the Corporation's floating rate mortgage portfolio and a decline in net fees recognized by MFC.

Assets under administration have grown significantly over three years due to capture of market share in the residential mortgage business and through portfolio acquisition in the other lines of business. Total mortgage and lease asset under administration for MCAP including affiliates have grown from $7.2 billion in 2000 to $17.6 billion at December 31, 2003.

Trends

Continued low interest rates fuel the Company's single-family residential mortgage operations. While an increase in rates would slow the single-family business, the commercial and residential construction businesses benefit from higher rates and the net investment income earned from the Company's investing activities improves.

The commercial mortgage market remains competitive and directly dependent on the Canadian economy. Investor appetite to fund commercial mortgages varies and financial service industry consolidation will no doubt impact this further. The Company has the leading commercial mortgage origination group in the country and numerous relationships with institutional lenders. The changes and consolidation in the industry bring new challenges but more importantly introduce new opportunities. As large financial institutions reorganize and outsource non-core business lines, there are opportunities for the Company to provide services.

The diversity of the Company's operations mitigates the effect of changes in the market place and stabilizes earnings over the long term.

FINANCIAL POSITION

Total assets at December 31, 2003 were $369.5 million, an increase of 13.0 percent, compared to total assets of $327.1 million in 2002. This increase in assets was expected, as the Company's capital grew over the year. Assets remain well diversified by type, geography, obligor and duration.

Shareholders' equity increased 5.8 percent year over year, from $58.4 million to $61.7 million at December 31, 2003, as earnings exceeded dividends and the Company issued shares under the dividend reinvestment plan (DRIP). Utilizing the DRIP from treasury enables the Company to invest at a regular pace, and provides the Company with predictable growth in capital over time. Earnings increased at a greater rate than the increase in capital, as the Company's return on equity increased from 10.8 percent in 2002 to 14.0 percent in 2003. The Company maintained the dividend level set in previous years at $0.68 per share.

Asset mix at December 31 was as follows:

	2003	2002
Cash and cash equivalents	**8.5%**	2.9%
Marketable securities	**2.1**	4.7
Bonds	**2.7**	–
Single-family mortgages	**48.7**	50.4
Residential construction loans	**14.6**	24.7
Non-residential construction loans	**–**	0.6
Commercial term mortgages	**.5**	0.3
Commercial loan	**1.4**	0.7
Leases	**2.9**	2.8
Other investments	**2.2**	2.2
Other assets	**16.4**	10.7
	100%	100%

Cash equivalents include treasury bills, bank deposits and bankers' acceptances. These investments ensure adequate liquidity to meet maturing debenture and new mortgage commitments.

Marketable securities comprise a diversified portfolio of real estate investment trusts, income trusts, royalty trusts and bonds. These investments are supported by the Company's equity base, and they provide for improved returns and the diversification of the Company's investment portfolio. The Company's investment policy limits marketable securities investment to $30 million.

Bonds include the Series C Bonds from the initial sale of residential construction mortgages to a securitization trust. The Company funded 100 percent of this bond on the initial sales as part of its capital management. Future issues of Series C Bonds may be sold to third parties as the program matures.

Single-family mortgages include uninsured mortgages with a loan-to-property value of 75 percent or less, and insured mortgages over 75 percent of property value. Mortgages are typically granted for terms of six months to five years and can be funded by debentures with similar maturities. During 2003, the Company acquired a portfolio of higher yielding sub-prime mortgages. The total single-family residential mortgage portfolio of $156 million includes $54 million in sub-prime mortgages. The Company limits its holding in sub-prime mortgages to $65 million.

Residential construction loans are made to home-builders to finance residential construction projects. These loans generally have a floating rate of interest and terms of one to two years. The Company's limit on conventional construction loans is 200 percent of regulatory capital. Non-residential construction loans may comprise up to one half of this limit. The maximum single conventional construction loan may not exceed $12 million.

Commercial term mortgages secure commercial properties and have a loan-to-property value of 75 percent or less. These mortgages have terms ranging from six months to five years. The Company limits its investment in these assets to 100 percent of regulatory capital. The maximum single commercial term mortgage may not exceed $5 million.

Other investments include equity investment in MCAP Service Corporation, a single-family mortgage origination and servicing company, and other companies within the mortgage industry that are of strategic interest to the Company.

Other assets include prepaid expenses, accounts receivable, capital assets, future tax assets, deferred costs, deferred purchase price receivable, goodwill and intangible assets.

Off Balance Sheet Arrangements

The Company enters into certain off balance sheet arrangements in the ordinary course of business. The following addresses the significant off balance sheet amounts.

Commitments

The Company commits to fund mortgages in advance of funding at an agreed upon interest rate. This creates an exposure to the Company from changes in interest rates during the commitment period. These commitments relate to mortgages for the Company's own investing operations or mortgages to be held for resale. The Company hedges a portion of the interest rate risk on commitments and mortgages held for resale through reverse repo transactions of Government of Canada bonds. Details of the Company's commitments and related hedges are included in notes 2, 4 and 18 of the consolidated financial statements.

Assets under Administration

The Company administers mortgage and lease assets for a variety of institutional investors and certain securitization trusts. The Company is responsible to collect and remit principal and interest payments and holds in trust, for a period of time, certain investor or borrower funds. Where the Company acts as agent and nominee or where the Company sells loans directly to third-party investors, the Company does not retain the credit or interest rate risk related to these financial assets.

In some cases the Company sells mortgages or leases to securitization trusts. The Company retains residual or intermediate positions in these securitization trusts. In some cases the Company provides over collateralization or credit support to the securitization trust. This subjects the Company to a portion of the credit and interest rate risk relating to these financial assets.

Details of the Company's asset administration and loan sales can be found in notes 2, 6 and 26 of the consolidated financial statements.

Contractual Obligations

The Company has contractual obligations to make principal and interest payments on debentures, a subordinated debenture and operating leases. The Company is also obligated to make certain payments, based on operating results, to the former principals of the ICI Mortgage group. Details of these contractual obligations can be found in the table below and in notes 18 and 25 of the consolidated financial statements.

Contractual obligations	[illegible]	[illegible]	[illegible]	[illegible]
Debentures	[illegible]	[illegible]	[illegible]	[illegible]
Subordinated debentures	[illegible]	[illegible]	[illegible]	[illegible]
Leases	[illegible]	[illegible]	[illegible]	[illegible]
Total	$ [illegible]	$ [illegible]	[illegible]	[illegible]

**Included at face value.*

Transactions with Related Parties

In the normal course of business, the Company purchases and sells certain corporate services, mortgage origination and mortgage administration services from the related party operations of MSC and MCLP. During 2003, the Company purchased $5.2 million from MSC and $525,000 from MCLP, while it sold $2.7 million to MSC and $1.6 million to MCLP.

Subsequent to year-end, the Company settled an amount of $7.5 million relating to two guarantees provided by Interior Capital Corporation (ICC). The Company acquired ICC on January 1, 2000 as part of a merger transaction. The merger transaction documents provided that the vendor shareholders of ICC would pay all costs incurred by the Company pursuant to the representations and warranties made by the vendor shareholders at the time of the merger. Pursuant to the merger transaction documents, the Company has signed agreements with the vendor shareholders of ICC to recover the costs related to the settlement of these guarantees and to date had received $3.5 million. For further information see Note 31 of the financial statements.

Funding

The Company issues debentures, insured by CDIC, largely to individuals. The Company matches the repricing of its assets with its liabilities. Through its practice of interest rate risk matching, the Company is positioned to manage changes in interest rates. Matching helps ensure that earnings will not be materially affected as a result of changes in interest rates. Note 18 to the consolidated financial statements provides more information on the balance sheet sensitivity to interest rate changes.

Asset Origination, Management and Sales

The Company, through its subsidiary, affiliate and joint venture operations, is involved in the origination, underwriting, servicing and funding of residential mortgages, residential construction loans, commercial mortgages, commercial term mortgages, and equipment leases. The Company originates loans for the following purposes:

- As agent and nominee for third-party investors.
- For the Company's own investing operations. These mortgages may be sold from time to time for capital management purposes, or to take advantage of market opportunities.
- As an aggregator for third-party investors. These mortgages are held for resale for a brief period of time and then sold to third-party investors.
- For the purpose of securitization.

Asset Management

The majority of the loans originated by the Company are committed and funded by third-party investors, with the Company acting as agent and nominee. The Company is not the beneficial owner of these mortgages, so they are not recorded on the Company's balance sheet. Since the Company does not own the mortgages, there is no sale recorded, nor is there recognition of gain upon the sale of the mortgages. The Company earns origination and servicing fees on these loans.

Asset Sales

As a mortgage investment corporation, the Company commits and funds loans for its own investing operations. The Company earns interest and fees on these loans. From time to time, the Company sells these loans to third-party investors. The Company, through its subsidiary, MFC, also aggregates loans for resale directly to third-party investors. The Company hedges a portion of the commitment risk and the interest rate risk relating to the mortgages held for resale. The Company records a gain or loss at the time of sale of these loans, which is equal to the fair value of the proceeds received, less the carrying value of the loans.

The Company sells certain mortgage loans and commercial leases to securitization entities. Securitization is a process whereby financial assets are sold to entities, usually trusts, and such entities issue interest-bearing notes. Contracts with securitization entities provide for the payment over time to the seller of the excess of interest and fees, from the financial assets, over the yield paid on the notes, less credit losses and other administrative costs. The amount of gain ultimately recognized over time is dependent on credit losses, prepayment speeds, and discount rates commensurate with the risks involved. In virtually all loan sales, the Company retains the right and obligation to service the mortgages and leases.

When developing its securitization programs, the Company has carefully considered the asset transfer accounting rules and the proposed rules governing the consolidation of securitization trusts or variable interest entities. MCAP believes it is important to ensure that the Company is in compliance with the maximum asset to capital measures required by regulations. The Company has structured these asset transfers to qualify as sales, and thus removes these assets from the balance sheet at the time of the transfer. The Company has also considered the proposed rules for variable interest entities and believes that it will not be required to report consolidated results from any securitization trust in which the Company holds a beneficial interest, or with which it transacts sales of assets. See Note 2 in the consolidated financial statements for further information regarding variable interest entities.

Capital Adequacy

The Company has two significant capital tests that must be closely monitored. As a mortgage investment corporation, the Company is limited by the Income Tax Act (Canada) to a liability to assets in excess of liabilities test of 5:1, based on its unconsolidated balance sheet at tax values. As a federally regulated financial institution, the Office of the Superintendent of Financial Institutions has granted the Company a 9:1 ratio of consolidated regulatory assets to consolidated regulatory capital. The ratio is significantly lower than the standard 20:1 ratio granted to the major banks. Note 23 in the consolidated financial statements further details the actual leverage ratio at December 31, 2003.

The Company operates and manages its balance sheet according to both of the above noted ratios, and is governed by the ratio that is most constraining during a given period of time. The Company's lower leverage, combined with its relatively conservative asset mix, reduces the risk of cyclical earnings or loss of book value.

Liquidity

The Company closely monitors its liquidity position to ensure it has sufficient cash to meet liability obligations as they become due. In general, the Company maintains liquid investments in excess of 20 percent of debentures maturing within 100 days. In addition, all marketable securities and single-family mortgages are readily marketable within a time-frame of one to three months, thus providing the Company with added flexibility to meet liquidity needs. The Company has access to capital through its ability to issue CDIC insured debentures. MCAP's liquidity position and its access to capital markets support the Company's ability to meet current and future commitments. There are no contingencies or known events that are likely to materially affect the Company's position.

RISK MANAGEMENT

MCAP is growing rapidly and operates in a constantly changing regulatory and economic environment. As a result, the Company's management and the Board of Directors are particularly diligent in their consideration of issues of risk. The Company's goal is not to eliminate risk, as this would result in significantly reduced earnings, but rather to be proactive in risk assessment and management of risk, to gain a strategic advantage and ultimately drive enhanced shareholder value.

The Company views and assesses risk on an enterprise-wide level. The Company's definition of enterprise-wide risk management has three main focal points:

- Controlling the impact of adverse events on the Company;
- Managing the inherent uncertainties that impact the achievement of its operational performance; and
- Pursuing opportunities to achieve a competitive advantage and increase shareholder value.

The Company recognizes that to manage its business risk effectively, the enterprise risk management process must be integral to the MCAP culture. For this reason, the Company has implemented a comprehensive enterprise-wide risk management framework. The Enterprise Risk Management Department is responsible for planning, directing and controlling the impact on MCAP of risks arising from its operations. This function reports to the Chief Risk and Investment Officer.

The Company's approach to enterprise-wide governance emphasizes that responsibility for the quality of processes, policies, procedures, controls, and internal reporting belongs to senior management on a day-to-day basis, while the responsibility for oversight and guidance rests with the Board of Directors.

The Company is exposed to a number of risks that can adversely affect its ability to achieve its business objectives or execute its business strategies, or that could result in a loss of earnings, capital or reputation. The Enterprise Risk Management Department, working with the other risk management control functions, has developed a comprehensive, systematic and disciplined risk management process for proactively identifying, assessing, managing and controlling the significant strategic, business and process level risks inherent in the business strategy and operations at any point in time.

In the normal course of business, the Company is exposed to various operational risks, in particular, interest rate risk and credit losses. The Company mitigates these risks through diligent management of assets and liabilities and by investment diversification. The Company fosters a "risk management culture," in which the individual who manages a business activity is expected to identify, assess and manage the significant risks associated with the activity.

Credit losses occur when a borrower fails to meet its obligations to the Company and the value realized on sale of the underlying real estate or equipment deteriorates below the loan amount. All personnel are subject to limits on their ability to commit the Company to credit risk. Credit and commitment exposure is closely monitored through a reporting process that includes a formal quarterly review, involving senior management and the Investment Committee of the Board of Directors.

Furthermore, the Company's exposure to credit risk is managed through risk management policies and procedures that emphasize the quality and diversification of the Company's investments. The Company's policies establish limits on concentration by asset class, rating, geographic region, dollar limit and borrower. By managing and matching the terms of mortgages and debentures so that they offset each other, the Company reduces risks associated with interest rate changes. The Company's Asset and Liability Management Committee reviews and manages this risk on a weekly basis. Management reports quarterly to the Board of Directors on its compliance with the Company's matching criteria.

Market risk related to marketable securities is managed through prudent investment selection and diversification by security and industry.

Regulatory Compliance

The Chief Compliance Officer ensures that management understands the impact of all relevant legislation affecting the business, assesses compliance with current and pending legislation, and works with management to address any gaps in policies and procedures. The Company has implemented a Legislative Compliance Management System that ensures all managers assess their compliance with relevant legislation on a semi-annual basis. The Chief Compliance Officer and the Vice President of Enterprise Risk Management liaise with regulators to keep them apprised of the Company's progress and changes to its business. The Chief Compliance Officer reports quarterly to the Chairman of the Conduct Review and to the Corporate Governance Committee of the Board of Directors. The Company has also taken proactive steps to ensure its readiness for the new Chief Executive Officer – Chief Financial Officer certification of the Company's financial reporting and disclosure controls.

Internal Audit

The Company has an Internal Audit function headed by the Chief Audit Officer, who has unrestricted access to the Company operations, senior management and the Chairman of the Audit Committee of the Board of Directors. The Chief Audit Officer performs an evaluation of business risk and then undertakes internal audits of those areas that are deemed to be of greatest risk. The Chief Audit Officer audits the effectiveness of internal control procedures of the Company and conducts independent assessments of the Enterprise Risk Management function and the effectiveness of the Legislative Compliance Management System. The Chief Audit Officer reports quarterly to the Audit Committee of the Board of Directors.

In addition, the External Auditors review the effectiveness of internal controls to the extent necessary to conduct an audit of the annual financial statements, and they report to the Audit Committee of the Board of Directors semi-annually on matters that come to their attention. They also conduct audits as required by our investors and regulators, which includes a detailed review of certain controls relating to administered assets and segregated trust moneys.

Ultimately, risk management is controlled at the highest level of the Company. The Board of Directors reviews and approves all risk management policies and procedures with respect to asset and liability mismatch risk, liquidity risk and credit risk. Without exception, all other key risk exposures are reported to the Board of Directors by management.

COMMUNITY INVOLVEMENT

MCAP is committed to giving back to the communities in which it does business, mainly through supporting two worthwhile charitable organizations, the United Way and Habitat for Humanity. The Company supports the goals of these organizations. They are both dedicated to providing a better quality of life for those members of society who need a helping hand.

Every year, MCAP's employees across Canada actively campaign for the United Way. The Company fully supports the time and the efforts contributed by employees, and demonstrates commitment by matching employee contributions to the program, dollar for dollar.

Habitat for Humanity is involved in constructing and providing houses to eligible families who might not otherwise be able to own their own home. MCAP provides financial support and staff support for the construction of housing.

OUTLOOK

During a time of turmoil in the equity markets, uncertainty in North American corporate governance and risks in the geopolitical environment, MCAP remained quietly successful. A prolonged low interest rate environment has provided significant challenges to our ability to earn investment income. However, the Company's capital management and sound strategic plan combined with employees committed to success have continued to deliver profitable results. New innovative products have enabled the Company to maintain its yields in this low interest rate environment. The Company's administered assets continue to grow, providing predictable fee income over time.

The Company's stated vision is "To be the first choice for financial solutions in our chosen markets." When the Company chooses to enter a market, it does so carefully, after weighing the potential risks and rewards to its business and profitability. The Company chooses to compete only in those markets where it can provide high quality service, valuable products, and strength in reputation that would make MCAP the customer's preferred choice. The Company has diversified its revenue sources in markets where it holds a strong competitive position, in order to achieve long-term sustainable earnings, and measured, steady growth.

MCAP cultivates an environment that promotes operational excellence and top performance. MCAP's experienced employees provide stability and help maintain a high level of confidence among investor and borrower clients, regulators and other stakeholders. Customers do business with MCAP because of the speed and quality of service, its breadth of access to capital markets and its ability to originate, underwrite, fund and service mortgage and leasing products in a seamless and professional manner. These are some of the Company's primary strengths.

Over the past years, MCAP has benefited from strong earnings delivered by its investing operations. With an increase in leverageable capital, as a result of the Company's proposed merger with CDP Capital – Mortgages, the Company expects to grow these earnings further. The Company has invested a significant portion of its funds in variable rate mortgages, funding a portion of these investments from capital. Furthermore, the Company earns interest on float balances including escrow and cash collateral amounts. Therefore, while an increase in interest rates may slow the residential construction and resale markets, the Company is positioned to benefit greatly from a moderate increase in interest rates.

The Company will continue to grow its fee-based revenue, which is driven by higher origination volumes and increased assets under administration. The structured finance programs developed in 2003 provide critical funding sources that complement our current investor base and provide the platform for growth in the immediate future. The proposed merger between the Company's mortgage and leasing operations and the mortgage operations of CDP Capital – Mortgages, is expected to make the combined group an even more significant player in the Canadian mortgage and leasing markets. The Company expects steady growth in profitability as these operations benefit from their complementary products and services. Together, these operations can be expected to bring new, innovative financial products to market.

There are opportunities to grow the leasing business in certain under-serviced markets. The leasing industry is undergoing dramatic change similar to that which took place a few years ago in the mortgage industry. Brokers are gaining market share in new originations, and consolidation is taking place among leasing companies with marginal operations. As the industry deals with these changes, the Company believes new and unique opportunities will arise to meet needs in niche markets and significantly grow the business.

The commercial mortgage market remains competitive and directly dependent on the Canadian economy. Investor appetite to fund commercial loans varies. In addition, industry consolidation in the life insurance business and potential bank mergers will no doubt have an impact on the commercial market. MCAP has the leading commercial origination group in the country and maintains numerous relationships with institutional lenders. The changes and consolidation ahead in the industry bring risk, but just as surely will present opportunities. For example, as large life insurance institutions reorganize and outsource non-core business lines, there are opportunities for MCAP to provide services.

The residential construction lending business remains competitive and complex. MCAP has an experienced group in this area and is well positioned to compete and grow this business. With the addition of the construction loan securitization program, this business is growing.

The Company has continued to enjoy excellent results in the single-family residential businesses of MCAP Service Corporation and MCAP Mortgage Corporation. Continued low interest rates and strong new housing and resale markets have fuelled record volumes. The competition in this market has increased as borrowers are using mortgage brokers and direct online banking as alternative ways to reduce their borrowing costs. Furthermore, banks and lending institutions are exploring non-traditional ways to distribute and service their products in order to reduce costs and increase their customer base. MCAP has benefited from these changes. The Company has a large network of broker relationships and the growth in this market has increased our market share.

In the coming year, MCAP will focus on profitable and stable growth. The proposed merger with CDP Capital – Mortgages is expected to further enhance our ability to generate quality financial products and to stay centred on meeting customer needs. The MCAP management team will remain intact in the combined operations and, together with the Board of Directors, will drive the future direction of the Company.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The consolidated financial statements, the MD&A and all quarterly financial information presented in the Annual Report are prepared on a consistent basis and in accordance with Canadian generally accepted accounting principles (GAAP), including interpretations of GAAP by the Company's regulator, the Office of the Superintendent of Financial Institutions of Canada.

The notes to the Company's consolidated financial statements provide detailed information on the Company's significant accounting policies, the method of applying those policies, and the material components of the amounts in the consolidated balance sheet, statement of income and retained earnings, and cash flow statement. The policies discussed below are considered particularly important, as they require management to make judgements involving estimations. The Company has control procedures to ensure these policies are applied consistently and that the policies are independently reviewed on at least an annual basis. Changes to accounting policies are made only after an appropriate amount of research and discussion has occurred and independent advice is obtained. Estimates are considered carefully and reviewed at an appropriate level within the Company. The Company believes the estimates used in determining its assets and liabilities are appropriate.

Allowance for Credit Losses

The allowance for credit losses reduces the carrying value of mortgage and leasing assets to provide for an estimate of the principal amounts borrowers may not repay in the future. In assessing the estimated realizable value of assets, the Company must rely on estimates and exercise judgement regarding matters for which the ultimate outcome is unknown. A number of factors can affect the amount the Company ultimately collects, including the quality of its own underwriting process and credit criteria, the diversification of the portfolio, the underlying security relating to the loans, and the overall economic environment. The Company has detailed underwriting and credit approval processes and procedures. However, future changes in circumstances could materially affect the Company's future provisions for credit losses from those provisions determined in the current year, and there could be a need to increase or decrease the allowance for credit losses. Details of the Company's accounting policies and balances of the allowances for credit losses can be found in Notes 2, 4 and 5 in the consolidated financial statements.

Asset Sales and Securitization

The Company sells certain mortgage and leasing assets to third-party investors and to securitization trusts. When these assets are sold, the Company records a gain (loss) on the sale, which is partly dependent on the estimation of the future cash flows from the transferred assets, the future interest costs of the securitization structure, credit losses and administration costs. Actual cash flows may differ significantly from those estimated by management. If management's estimate of future cash flow had been different, the gains on asset sales or securitization would also have been different.

In some cases, the Company retains an interest in the assets or the residual cash flows of the securitized assets or may provide over-collateralization or credit support to the securitization trust. Changes in circumstances may require a write-down of these retained interest assets, or an increase to liabilities relating to credit support guarantees.

Goodwill

The Company records goodwill on acquisitions in instances where the amount paid exceeds the fair value of the net identifiable assets. This goodwill is tested at least annually to determine if the carrying value is less than fair value. The fair value of the goodwill is determined using valuation techniques that consider discounted cash flows, price/earnings multiples and budgeted earnings. Management must apply prudent judgement in the selection of the approach to determining fair value and in making any necessary assumptions. Changes in these assumptions could result in a decline in the estimated fair value and an impairment write-down. Details of the Company's accounting policies and balances of goodwill can be found in Notes 2, 9 and 10 in the consolidated financial statements.

Income Taxes

The provision for income taxes is based on the Company's interpretation of the relevant tax rules and the estimation of the period of reversal of certain timing differences between the financial reporting and tax bases of assets and liabilities. Differences in interpretation of tax rules or the period of reversal of timing differences could result in a change to the income tax provision in the future. As a mortgage investment corporation, the Company can deduct dividends paid to the shareholders from its calculation of taxable income. As a result, the Company can mitigate some of the risk of future changes to the tax provision through the payment of dividends at that time. Details of the Company's accounting policies and balances relating to income taxes can be found in Notes 2 and 17 in the consolidated financial statements.

2003 consolidated financi

MANAGERS' RESPONSIBILITY FO

The accompanying consolidated financial statements of MCAP Inc. (the "Company") are the responsibility of management and have been approved by the Board of Directors. Management is responsible for the information and representations contained in these financial statements, the Management's Discussion and Analysis of Operations and all other sections of the annual report. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP) and include interpretations of GAAP by our regulator, the Superintendent of Financial Institutions Canada.

Appropriate systems of internal control, policies and procedures have been maintained to provide reasonable assurance that the Company's financial records are complete and accurate and that assets are safeguarded against loss from unauthorized use or disposition.

The Superintendent of Financial Institutions Canada makes such examination and enquiry into the affairs of MCAP as he may deem necessary to satisfy himself that the provisions of the Loan and Trust Companies Act are being duly observed for the benefit of depositors and that the Company is in sound financial condition.

The Board of Directors is responsible for ensuring that management fulfils its responsibility for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. These responsibilities are carried out primarily through an Audit Committee of unrelated directors appointed by the Board of Directors. The Chief Audit Officer and Chief Compliance Officer review internal controls, control systems and compliance matters and have full and independent access to the Audit Committee.

The Audit Committee meets periodically with management and the external auditors to discuss internal control over the financial reporting process, auditing matters and financial reporting issues. The Audit Committee reviews the consolidated financial statements and recommends them to the Board of Directors for approval. The Audit Committee also recommends to the Board of Directors and Shareholders the appointment of external auditors and approval of their fees.

The consolidated financial statements have been audited by the Company's external auditors, Ernst & Young LLP, in accordance with Canadian generally accepted auditing standards. Ernst & Young LLP has full and free access to the Audit Committee.

Derek Norton
President and Chief Executive Officer

L. S. Jenkins

Lorne Jenkins
Vice-President and Chief Financial Officer

AUDITORS' REPORT

To the Shareholders of MCAP Inc.

We have audited the consolidated balance sheets of MCAP Inc. as at December 31, 2003 and 2002 and the consolidated statements of income and retained earnings and cash flow for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Chartered Accountants
Toronto, Canada
March 2, 2004

Consolidated balance sheet

[illegible] ember 31 (Dollars in thousands)

	Note	2003	2002
Assets			
Investments			
Cash and cash equivalents	3	**$ 31,395**	$ 9,436
Mortgages	4	**240,937**	250,935
Other investments	5, 6	**36,776**	31,652
		309,108	292,023
Accounts receivable	7, 31	**17,539**	4,790
Capital assets	8	**4,843**	5,778
Goodwill and intangible assets	9	**10,502**	8,722
Loans receivable	11	**15,767**	8,452
Other assets	12	**11,718**	7,294
		$ 369,477	$ 327,059
Liabilities and Shareholders' Equity			
Liabilities			
Debentures	13	**$ 267,446**	$ 222,619
Accounts payable and accrued charges	7, 31	**22,019**	16,681
Loans payable	14	**650**	11,935
Subordinated debenture	15	**17,621**	17,441
		307,736	268,676
Shareholders' equity			
Share capital	16	**58,980**	57,405
Retained earnings		**2,761**	978
		61,741	58,383
		$ 369,477	$ 327,059

See accompanying notes

On behalf of the Board:

Derek Norton
President and Chief Executive Officer

David G. Broadhurst
Director, Chairman of the Audit Committee

consolidated statement

Year Ended December 31 (Dollars in th

	Note	2003
Investment Income		
Mortgage interest income		$ 17,162
Interest on cash and cash equivalents		1,982
Leasing income		5,723
Other income		5,577
		30,444
Financial Expenses		
Interest expense		9,812
Other expenses		2,378
		12,190
Net investment income		18,254
Fee income	19	13,835
Related interest and fees		(2,448)
Net fee income		11,387
Revenue from operations		29,641
Operating Expenses		
Salaries and administrative		17,072
Occupancy		1,573
Information systems		2,603
		21,248
Income before income taxes		8,393
Provision for income taxes and large corporation taxes	17	146
Net income		$ 8,247
Retained earnings, beginning of year		978
Dividends		(6,464)
Retained earnings, end of year		$ 2,761
Earnings per share	21	
Basic earnings per share		$ 0.85
Diluted earnings per share		$ 0.83
Dividends per share		$ 0.68
Weighted average # of shares (000's)		9,693
Weighted average # of diluted shares (000's)		9,922

See accompanying notes

isolidated cash flow statement

1 (Dollars in thousands)

	2003	2002
Cash Provided by (used for):		
Operating Activities		
Net income	$ 8,247	$ 5,430
Adjusted for non-cash items:		
Equity income from partly owned company	(817)	(961)
Provision for losses	485	1,874
Amortization of capital assets	1,508	1,828
Amortization of intangible assets	189	158
Amortization of other assets	2,043	1,106
Amortization of debenture discount	180	151
Amortization of mortgage premiums (discounts)	14	(34)
Future tax assets	(771)	(105)
Capitalized interest on investor loans	(272)	(254)
Gain on sale of mortgages and leases	(4,726)	(3,590)
(Increase) decrease in non-cash working capital:		
Accounts receivable	(5,249)	(550)
Accounts payable and accrued charges	(2,251)	5,152
Cash flows (for) from operating activities	(1,420)	10,205
Investing Activities		
Marketable securities	(2,467)	(4,504)
Mortgage advances	(528,706)	(270,484)
Mortgage reductions	549,481	192,551
Mortgages held for resale	(7,995)	(4,160)
Leases	(94)	(3,968)
Additions to capital assets	(573)	(3,991)
Additions to goodwill and intangible assets	(1,384)	(5,703)
Increase in loans receivable	(7,315)	(8,452)
Additions to other assets	(5,696)	(5,011)
Cash flows for investing activities	(4,749)	(113,722)
Financing Activities		
(Decrease) increase in loans payable	(11,285)	2,765
Issue of debentures	471,353	462,834
Repayment of debentures	(426,526)	(393,861)
Issue of common shares and warrants	990	11,084
Dividends	(6,404)	(6,099)
Issue of subordinated debenture	-	17,290
Cash flows from financing activities	28,128	94,013
Increase (decrease) in cash and cash equivalents	21,959	(9,504)
Cash and cash equivalents, beginning of year	9,436	18,940
Cash and cash equivalents, end of year	$ 31,395	$ 9,436

	2003	2002
Supplementary Information		
Interest paid during the year	$ 11,408	$ 11,061
Taxes paid during the year	$ 858	$ 1,043

See accompanying notes

notes to consolidated fi

December 31, 2003 (Dollar amounts i

1. BASIS OF PRESENTATIO

MCAP Inc. (the "Company") is a Loan Company under the Trust and Loan Companies Act (the "Trust Act") and a Mortgage Investment Corporation under the Income Tax Act (Canada) (the "Tax Act").

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, MCAP Financial Corporation (MFC), MCAP Securities Inc. and MTC Leasing Inc. (MTCL).

The results of MFC include 50% of the results of MCAP Commercial Limited Partnership (MCLP), a joint venture operation between MFC and Cadcap Inc. (Cadcap). MFC is the general partner of MCLP. The accounts of MCLP are proportionately consolidated in these financial statements. The Company's proportionate share of transactions with MCLP has been eliminated.

The Company's 20% interest in MCAP Service Corporation (MSC) and its subsidiary MCAP Mortgage Corporation (MMC) is accounted for using the equity method.

The purchase method has been used to account for all acquisitions. Intercompany balances and transactions of fully consolidated subsidiaries are eliminated.

2. SUMMARY OF SIGNIFI

The Company prepares consolidated financial statements in accordance with Canadian generally accepted accounting principles (GAAP), including interpretations of GAAP by its regulator, the Office of the Superintendent of Financial Institutions Canada (OSFI).

Measurement Uncertainty
Management of the Company exercises its best judgement with regard to certain estimates and assumptions, which affect the reported amounts of revenue, expenses, assets, and liabilities. Specific amounts subject to such judgement include provisions for future credit losses, prepayment rates, provisions for future administration costs and estimated residual realization values. Actual results could differ from Management's estimates.

Cash and Cash Equivalents
Cash and cash equivalents include balances with banks and short-term investments with maturity dates of less than 90 days from the date of acquisition. Cash and cash equivalents are stated at cost plus accrued interest.

Marketable Securities
Marketable securities are stated at cost less any write-down for decline in value, which is other than temporary.

Mortgages and Mortgages Held for Resale
Mortgages held directly by the Company are carried at the amortized cost including origination costs, plus accrued interest, less unearned income and an allowance for loan losses.

Mortgages held for resale by the Company as part of trading inventory are carried at the lower of cost or market value.

Equity Investments
Equity investments where the Company can exercise significant influence are recorded on the equity accounted basis. The Company records equity earnings equal to its proportionate share of the equity investment's net income. Equity investments where the Company does not exercise significant influence are recorded at cost.

Impaired Loans
Interest on mortgages is accrued as earned until such time as a loan is classified as impaired. At that time, a specific provision is made to reflect Management's estimate of realizable amounts. Impaired loans are restored to an accrual basis when principal and interest payments in arrears become current and there is reasonable assurance as to ultimate collectibility.

Impaired loans include non-insured loans which are more than 90 days in arrears or are less than 90 days in arrears but for which Management does not have reasonable assurance that the full amount of principal and interest will be collected in a timely manner. An insured loan is considered impaired when the loan is 365 days past due, whether or not collection is in doubt.

Restructured Loans

Restructured loans are those loans where, because of the weakened financial condition of the borrower, the terms have been modified. These loans are carried at the net present value of future cash flows, discounted at the contractual interest rate in effect immediately prior to the restructuring. Restructured loans are not included in impaired loans if the borrowers have complied with the terms and Management has reasonable assurance that principal and interest under the new terms will be collected in a timely manner.

Allowance for Loan Losses

An allowance for mortgage loan losses, consisting of specific and general provisions, is maintained at a level that, in Management's judgement, is adequate to absorb all credit related losses in the Company's portfolio. Specific provisions include all of the accumulated provisions for losses on particular assets required to reduce the related assets to estimated realizable value. The general provision includes provisions for losses which are prudent in nature and cannot be determined on an item-by-item basis.

The allowance is increased by provisions for losses, which are charged against income, and reduced by write-offs, net of recoveries. Write-offs are generally recorded after all reasonable restructuring or collection activities have taken place and the possibility of further collection is considered to be remote.

In Management's judgement, no abnormal credit risk exists and the levels of loan loss provisions are adequate to absorb all expected credit related losses in the Company's portfolio, given existing conditions.

Leases

Leases are recorded at their present value using the rate implicit at the inception of the lease. An estimate of future credit losses attributable to the leases is charged against income at lease inception.

Non-performing Leases

Lease contracts, which become more than 120 days in arrears, are declared non-performing and no further income is recorded on such contracts. Other contracts may also be declared non-performing such as in the case of insolvencies or bankruptcies. All non-performing leases are written down to their estimated net realizable value.

Asset Origination, Management and Sales

The Company is involved in origination, underwriting, servicing and funding residential mortgages, residential construction loans, commercial mortgages, commercial term loans, and equipment leases. The Company originates loans for the following purposes:

- As agent and nominee for third-party investors.
- For the Company's own investing operations. These loans may be sold from time to time for capital management purposes or to take advantage of market opportunities.
- As an aggregator for third-party investors. These loans are held for resale for a brief period of time and then sold to third-party investors.
- For the purpose of securitization.

Asset Management

The majority of the loans originated by the Company are committed and funded by third-party investors and the Company acts as agent and nominee. The Company is not the beneficial owner of these loans. In such cases, these loans are not recorded on the Company's balance sheet. As the Company does not own the loans, there is a no sale recorded or gain on sale recognition. The Company earns origination and servicing fees on these loans.

Asset Sales

For transfers and sales that have occurred after July 1, 2001, the Company accounts for the sale of assets where control over the assets is relinquished in accordance with *CICA Accounting Guideline 12.*

As a Mortgage Investment Corporation, the Company commits and funds loans for its own investing operations. The Company earns interest and fees on these loans. From time to time, the Company sells these loans to third-party investors. The Company also aggregates loans for resale directly to third-party investors. The Company hedges a portion of the commitment risk and the interest rate risk relating to the mortgages held for resale. The Company records a gain or loss at the time of sale of these loans equal to the fair value of the proceeds received less the carrying value of the loans. The Company receives full cash consideration at the time of sale for a majority of such loan sales. In other cases, a portion of the proceeds is paid over time.

The Company sells certain mortgage loans and commercial leases to securitization entities. Securitization is a process whereby financial assets are sold to entities, usually trusts, and such entities issue interest-bearing notes. Contracts with

securitization entities provide for the payment over time to the seller of the excess of interest and fees, from the financial assets, over the yield paid on the notes less credit losses and other administrative costs (the deferred purchase price). Securitization income is recognized at the time of sale as the excess of the fair value of proceeds received, less the cost of the assets sold and less the fair value of any servicing liability. In some cases, the Company retains a subordinated retained interest in the securitization entity. This interest provides additional collateral to the senior note holders. The amount of the gain or loss recognized depends in part on the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the retained interests, based on their relative fair values at the date of transfer. To obtain fair values, quoted market prices are used if available. However, quotes are generally not available for retained interests and the Company generally estimates fair value based on the net present value of future expected cash flows, using management's best estimates of key assumptions – credit losses, prepayment speeds, and discount rates commensurate with the risks involved.

The Company retains the right and obligation to service the mortgages and leases in virtually all loan sales. Where the Company receives servicing fees at a rate that is less than or in excess of market, a servicing liability or servicing asset is recorded. Servicing liabilities are recorded at fair value and are recognized as a reduction in the gain on sale calculation. Servicing assets are recorded by allocating a portion of the carrying value of the financial assets transferred, based on the relative fair value of the servicing assets. The result of this allocation is an increase in the calculation of the gain on sale.

Senior retained interests in securitization entities are considered loan investments where the credit quality of the instrument is high. Interest is recognized on the accrual basis on these loan investments. Subordinated retained interests with high credit risk are considered debt securities and the interest on these investments is recorded using the effective yield method by amortizing the accretable yield over the life of the retained interest. The accretable yield is the difference between the total expected cash flows from the retained interest and its carrying value.

On a quarterly basis, the Company compares the carrying value of the retained interests to their fair value, determined based on discounted cash flow. When a decline in value is identified that is other than temporary, the affected carrying amount is written down to its fair value.

Variable Interest Entities

The CICA has issued *Accounting Guideline 15* defining the consolidation rules for variable interest entities (VIEs). These rules require the holder of the majority of variable interests of a VIE to consolidate the entity. Variable interests are defined as the exposure to both expected losses and expected gains. In the event of an equal sharing of expected losses and expected gains, the beneficiary with the majority of expected losses would be required to consolidate the VIE. These rules do not apply to VIEs considered Qualifying Special Purpose Entities. The effective implementation date of these rules has been deferred until November 1, 2004. The Company has considered these rules carefully in the development of its securitization programs and does not expect to consolidate any VIEs as a result of these new rules.

Revenue and Expense Recognition

(a) Relating to the Company's mortgage portfolio, the Company is entitled to fees for committing and funding the mortgage loans. A portion of these fees is allocated to the Company's mortgage operations and a portion represents part of the yield earned by the Company's investing operations. The portion of fees earned by the mortgage operations is recognized at the initial funding of the loans. The portion earned by the investing operations is deferred and amortized into income over the term of the mortgage.
(b) Amounts received on the buydown of mortgage interest rates are deferred and amortized over the term of the mortgage.
(c) Commissions paid on the issue of debentures are deferred and amortized over the term of the debenture.
(d) Mortgage administration fees are recorded as earned and are presented net of administration fees paid to other parties.
(e) Origination costs paid on the Company's mortgage portfolio are deferred and amortized over the term of the loan.
(f) Lease income is recognized on Company owned leases using the interest method. Financing earnings are recognized in income by applying a constant interest rate.

Capital Assets

Capital assets are recorded at cost. Amortization is recorded at the following rates:

Furniture and fixtures	5 years straight line
Computer hardware	3 years straight line
Computer software	One year to five years straight line
Leasehold improvements	Lease term and one renewal

Expenses incurred for the development or enhancement of computer operating and application systems for which an economic benefit can be determined, are deferred and amortized over the expected benefit period, to a maximum of five years. Amortization commences when a significant project phase is completed.

Future Income Taxes

The Company uses the liability method of tax allocation in accounting for income taxes. Under this method, future tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Foreign Exchange

Foreign currencies are translated into Canadian dollars at year-end rates of exchange for monetary items and at exchange rates prevailing at the respective transaction dates for both non-monetary foreign assets and liabilities, and income and expense items.

Transaction Costs

Incremental transaction costs relating to the issue of debt, the issue of capital, business combinations, asset acquisitions, and product program development are deferred to the extent the related transaction is “more likely than not” to proceed. Upon completion of the transaction, costs relating to the issue of debt are deferred and amortized against the related financing, costs related to the issue of capital are recorded as a capital transaction, and costs related to business combinations and asset acquisitions are added to the cost of the related business or asset. If a transaction is abandoned, the deferred costs are expensed in the period. Costs associated with product program development are amortized over the anticipated period of benefit.

Goodwill and Intangible Assets

The difference between the acquisition cost of a business and the fair value of the net tangible assets acquired is allocated first to intangible assets and the excess to goodwill. Servicing rights relating to acquired contracts are amortized over the term of the related contracts. Goodwill is not amortized. Intangible assets are considered impaired and are written down to their net recoverable amount when their net book value exceeds their estimated future net cash flows. Goodwill is considered impaired and is written down to fair value when the net book value of an acquired business exceeds its fair value. The carrying value of goodwill is reviewed annually or when an event occurs that “more likely than not” reduces the fair value of an investment.

Financial Instruments

The fair value of financial items is approximately equal to recorded amounts unless otherwise disclosed.

The following methods and assumptions were used to estimate the fair value of the on-balance sheet financial instruments:

Financial Instruments Valued at Carrying Value

Due to their short-term maturity, the carrying values of cash equivalents, accounts receivable and accounts payable and accrued charges approximate their fair values.

Marketable Securities

Fair values are based on quoted market prices, when available. If quoted market prices are not available, fair values are estimated using quoted market prices of similar securities.

Mortgages and Investor Loans

The fair values of mortgages and investor loans are estimated on a discounted cash flow basis that uses market interest rates currently charged for similar mortgages and loans at December 31 to expected maturity dates.

Equity Investments

The Company uses quoted market values for equity investments when available. Fair values for private investments are determined using discounted cash flow techniques using discount rates appropriate for the nature of the underlying businesses. In certain cases for private entities the Company is unable to obtain the information to perform these calculations on a practicable basis due to the nature or size of the underlying business. Management believes the fair value of these investments is in excess of carrying value.

Leases

The fair value of leases is estimated on a discounted cash flow basis that uses market interest rates currently charged for similar leases at December 31 to expected maturity dates.

Debentures

The estimated fair values of debentures are determined by discounting the contractual cash flows, using market interest rates currently offered for deposits of similar remaining maturities.

Derivative Financial Instruments

In the normal course of business, the Company enters into hedging transactions to manage interest rate risk on commitments and mortgages held for resale. The Company does not purchase or hold derivative financial instruments for speculative purposes. The Company monitors relationships between hedging instruments and associated hedged items. This monitoring includes identification of the specific mortgages held for resale, the nature of the risk being hedged, the hedge objective, and effectiveness of the hedge.

The Company utilizes derivative instruments designated as fair value hedges to manage the interest rate risk associated with commitments and mortgages held for resale. Recognition of the changes in the fair value of these derivative instruments is deferred and recorded in income in the period in which the hedged transaction occurs, offsetting the gain or loss on the mortgages upon sale.

Realized and unrealized gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, are deferred under other assets or accounts payable and accrued charges on the balance sheet and recognized in income in the period in which the underlying hedged transaction is recognized.

3. CASH AND CASH EC

	2003	
Corporate cash and cash equivalents (overdraft)	$ 6,409	[illegible]
Bankers' acceptances, term deposits and treasury bills	24,464	[illegible]
Accrued interest	20	[illegible]
	$ 30,893	[illegible]
Trust assets	34,205	[illegible]
Trust liabilities	(33,703)	[illegible]
Excess trust assets	$ 502	[illegible]
Cash and cash equivalents	$ 31,395	[illegible]

The Company maintains trust accounts on behalf of the financial institutions it represents. These funds include amounts held to fund mortgages, cash collateral balances held to secure letters of credit and escrow balances primarily for property taxes. The unused funds are invested in short-term deposits and the excess of trust assets over trust liabilities represents cash available to the Company.

4. MORTGAGES

	2003	
Conventional mortgages	$ 175,412	[illegible]
Insured mortgages	41,785	[illegible]
Mortgages held for resale	24,146	[illegible]
	241,343	[illegible]
Accrued interest	1,129	[illegible]
	242,472	[illegible]
Less: Allowance for credit losses	1,535	[illegible]
	$ 240,937	$ 2[illegible]
Fair value	$ 241,816	$ 253,667

At December 31, 2003 and 2002 the Company did not hold any individual mortgage or counter-party position in excess of 5% of total mortgages.

I, 2003 (Dollar amounts in thousands except for per share amounts)

The details of the mortgage loan provisions are as follows:

				2003
Allowance for Credit Losses	Beginning of Year	Additions (Recoveries)	(Write-Offs)	End of Year
Specific provisions	$ 580	$ (509)	$ -	$ 71
General provisions	1,539	96	(171)	1,464
	$ 2,119	$ (413)	$ (171)	$ 1,535

				2002
Allowance for Credit Losses	Beginning of Year	Additions	(Write-Offs)	End of Year
Specific provisions	$ 556	$ 106	$ (82)	$ 580
General provisions	1,044	572	(77)	1,539
	$ 1,600	$ 678	$ (159)	$ 2,119

At December 31, 2003, the Company had $1,405 of impaired loans (2002 – $2,306).

Outstanding commitments for future fundings of mortgages intended to be held for resale are $21,062 at December 31, 2003 (2002 – $15,571).

Outstanding commitments for future mortgage fundings are $131,246 at December 31, 2003 (2002 – $219,475). Interest rates on future mortgages are determined at the time of commitment. Outstanding commitments range for periods of up to 4 months in duration and have maturities ranging from 6 months to 5 years (2002 – 6 months to 5 years) with rates ranging from 4.5% to 6.9% (2002 – 3.71% to 8.5%).

OTHER INVESTMENTS

		2003	2002
Marketable securities	(a)	$ 7,812	$ 15,452
Bonds	(b)	10,106	–
Leases	(c)	10,627	9,058
Investor loans	(d)	3,997	3,725
Filogix Inc.	(e)	1,001	1,001
Equity accounted investments		3,233	2,416
		$ 36,776	$ 31,652

(a) Marketable securities

	2003	2002
Income, royalty and real estate investment trusts	$ 7,812	$ 10,188
Bond funds	-	5,264
	$ 7,812	$ 15,452
Fair value	$ 9,078	$ 16,210

(b) Bonds

	2003	2002
Bonds	$ 10,106	$ –
Fair value	$ 10,106	$ –

At December 31, 2003, Bonds includes $10,106 of Series C Bonds issued by a securitization entity, which bears interest at the bankers acceptance rate plus 2.75% (note 6).

(c) Leases

Leases consist of the following:

	Note	2003	[illegible]
Investment in leases		$ 5,080	$ 5,275
Lease assets held for securitization		3,366	3,716
Retained interests in securitized leases	6	4,686	3,21[illegible]
		13,132	[illegible]
Less: Allowance for credit losses		2,505	[illegible]
		$ 10,627	[illegible]

Fair value

	Note	2003	[illegible]
Investment in leases		$ 2,575	[illegible]
Lease assets held for securitization		3,500	[illegible]
Retained interests in securitized leases	6	5,651	[illegible]
		$ 11,726	[illegible]

The leases have a weighted average term of 40 months (2002 – 39 months) and a weighted average yield of 12.2% (2002 – 12.3%).

The Company's subsidiary MTCL originates and securitizes equipment leases. The Company provides allowances for credit losses, losses on unguaranteed residual values and administration costs, based on its experience. The Company's allowance for credit losses on leases held for its own investment is summarized below.

				2003
Allowance for Credit Losses	Beginning of Year	Additions	(Write-Offs)	End of Year
	$ 3,151	$ 868	$ (1,514)	$ 2,505

				[illegible]
Allowance for Credit Losses	[illegible]	[illegible]	[illegible]	[illegible]
	[illegible]	[illegible]	[illegible]	[illegible]

(d) Investor loans

	2003	[illegible]
Immigrant Investor Program	$ 3,900	[illegible]
Accrued interest	97	[illegible]
	$ 3,997	[illegible]
Fair value	$ 4,121	[illegible]

These loans are made to borrowers under the Quebec Immigrant Investor Program. These loans have a maturity of August 31, 2004, and bear interest of 7.33% per annum (2002 – 7.33% per annum).

(e) Filogix Inc.

The Company holds an investment in Filogix Inc., a private company, which is carried at cost, representing a less than 5% ownership interest in Series A preferred shares.

2003 (Dollar amounts in thousands except for per share amounts)

ASSET SALES

During 2003 and 2002, the Company sold residential mortgage loans, residential construction loans and commercial lease receivables. In the majority of those transactions, the Company retained servicing rights and obligations and subordinated retained interests. The value of such retained interests is subject to credit, prepayment, and interest rate risks on the transferred financial assets. Purchasers of transferred mortgage loans have no recourse to the Company. Under the terms of sale of leases to a securitization trust, a portion of the proceeds is paid to the Company over time and represents a retained interest in the securitized leases. In connection with direct sales of leases to an investor client, a letter of credit is provided on account of possible credit losses from the leases sold. The required letter of credit amount is based on a percentage of current leases outstanding and is recalculated quarterly.

During 2003, the Company initiated a residential construction mortgage loan securitization program. Under this program the Company originates, funds, and transfers loans to a securitization entity. The Company will receive fees for servicing the loans and retains subordinated interests in the securitization entity, to provide a portion of the credit enhancement for the program. The subordinated interests include Series C Bonds (note 5), which have been rated A by the Dominion Bond Rating Service, and other subordinate positions. While the Company sells approximately 25% of the mortgages to the securitization program and Warehouse Trust sells 75%, the Company retained 100% of the Series C Bonds on the initial sales as part of the Company's capital management strategy. Future issues of these Series C Bonds may be sold to third parties as the program matures. The Company holds a minority of the most junior interest in the securitization.

The following table sets out certain amounts recognized in the Company's consolidated financial statements related to mortgage and lease sales:

	Gains on Sales of Loans		Amortization of Servicing Liability	
	2003	2002	**2003**	2002
Residential mortgages	**$ 2,384**	$ 2,341	**$ -**	$ –
Commercial leases	**$ 2,342**	$ 1,249	**$ 1,542**	$ 1,406
Residential construction mortgages	**$ -**	$ –	**$ -**	$ –

	Retained Interests					
Carrying Value	Deferred Purchase Price Receivable		Investment in Securitization Entities		Servicing Liability	
	2003	2002	**2003**	2002	**2003**	2002
Residential mortgages	**$ 1,189**	$ 1,527	**$ -**	$ –	**$ -**	$ –
Commercial leases	**$ 4,686**	$ 3,218	**$ -**	$ –	**$ 2,071**	$ 2,047
Residential construction mortgages	**$ 2,929**	$ –	**$ 10,106**	$ –	**$ -**	$ –

Fair Value	Deferred Purchase Price Receivable		Investment in Securitization Entities		Servicing Liability	
	2003	2002	**2003**	2002	**2003**	2002
Residential mortgages	**$ 1,189**	$ 1,527	**$ -**	$ –	**$ -**	$ –
Commercial leases	**$ 5,651**	$ 3,900	**$ -**	$ –	**$ 2,071**	$ 2,047
Residential construction mortgages	**$ 2,929**	$ –	**$ 10,106**	$ –	**$ -**	$ –

Of the total residential mortgage sales in 2003, 37% involved sales where the Company has a retained interest (2002 – 68%).

Residential construction mortgages are variable rate loans sold at par and the fair value of the proceeds and retained interests are approximately equal to the carrying value of the loans at the time of sale. As a result, there is no gain or loss recorded on these loan sales.

The following table summarizes certain cash flows received from mortgage and lease sales for the periods ended:

	Residential Construction Mortgages	Residential Mortgages		Commercial Leases	
	2003	2003	[illegible]	2003	2002
Proceeds from sales	$ 24,738	$ 220,884	[illegible]	$ 39,429	$ 16,757
Receipt of deferred purchase price and servicing fees	$ 107	$ 715	[illegible]	$ 893	$ 1,331

The following table sets out credit information related to the Company's assets securitized or otherwise sold:

	2003		2002	
	Securitized Assets	Credit Losses	Securitized Assets	Credit Losses
Commercial leases	$ 69,029	$ 1,514	[illegible]	$ 1,049
Residential construction mortgages	$ 37,773	$ –		

Residential mortgages were sold without recourse. The deferred purchase price receivable represents direct claims against the purchasers of the mortgages and consequently the Company is not exposed to the credit risk of the assets sold.

The Company's credit exposure to lease assets securitized or otherwise sold as at December 31, 2003 is limited to the deferred purchase price receivable of $4,686 (2002 – $3,218) and a letter of credit of $2,500 (2002 – $1,750).

At December 31, 2003, the delinquency rate was 0.87% (2002 – 0.57%) for securitized leases.

The following table outlines the key economic assumptions used in measuring the retained interests and the sensitivity of the fair value of such retained interests as at December 31, 2003 to immediate 10% and 20% adverse changes in those assumptions. The sensitivity analysis is hypothetical and changes in each key assumption may not be linear. The sensitivities in each key variable have been calculated independently of changes in the other key variables. Actual experience may result in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce certain sensitivities.

	Residential Construction Mortgages	Residential Mortgages	Commercial Leases
Retained interests			
Deferred purchase price receivable	$ 2,929	$ 1,189	$ 5,651
Investment in securitization entities	10,106	–	–
Servicing liability	–	–	(2,071)
	$ 13,035	$ 1,189	$ 3,580
Impact of:			
Prepayment rate (%)	0%	7%–11%	0%
10% adverse change	$ –	$ 128	$ –
20% adverse change	$ –	$ 149	$ –
Interest rate (%)	2.77%	–	5.5%
10% adverse change	$ –	–	$ 160
20% adverse change	$ –	–	$ 320
Expected credit losses (%)	0.35%	–	2%
10% adverse change	$ 7	–	$ 145
20% adverse change	$ 14	–	$ 290
Discount rate (%)	7.4%	5%	9.1%
10% adverse change	$ 99	$ 10	$ 50
20% adverse change	$ 195	$ 20	$ 100

The residential construction mortgage securitization program is an open ended, revolving structure with variable rate interest costs and revenues. As a result, prepayment rates and interest rates have minimal impact on the values of the retained interests.

3 (Dollar amounts in thousands except for per share amounts)

ACCOUNTS RECEIVABLE/PAYABLE

(a) Accounts receivable

	Note	2003	2002
Related party receivable – MCLP		$ 5,305	$ 1,924
Other related party receivables	31	7,500	155
Other receivables		4,734	2,711
		$ 17,539	$ 4,790

(b) Accounts payable and accrued charges

	Note	2003	2002
Accounts payable and accrued charges	31	$ 17,264	$ 10,079
Deferred revenue		4,554	5,779
Related party payables		201	823
		$ 22,019	$ 16,681

The Company purchases/sells certain corporate services and mortgage origination and loan administration services from/to MSC. During 2003, the Company purchased $5,237 (2002 – $6,152) and sold $2,702 of services (2002 – $2,508).

The Company purchases/sells certain corporate services and mortgage origination and loan administration services from/to MCLP. During 2003, the Company purchased $525 (2002 – $379) and sold $1,638 of services (2002 – $4,348).

Lease inducements with a carrying value of $1,495 (2002 – $1,550) net of amortization of $232 (2002 – $88) are included in accounts payable and accrued charges.

CAPITAL ASSETS

	2003		2002	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Furniture and fixtures	$ 1,807	$ 1,155	$ 2,993	$ 2,294
Computer hardware	2,450	1,795	2,248	1,501
Computer software	4,306	2,636	4,366	1,998
Leasehold improvements	2,553	687	2,453	489
	$ 11,116	$ 6,273	$ 12,060	$ 6,282
Net book value	$ 4,843		$ 5,778	

GOODWILL AND INTANGIBLE ASSETS

	2003	2002
Servicing rights	$ 1,877	$ 1,877
Accumulated amortization	(394)	(205)
	$ 1,483	$ 1,672
Goodwill	9,019	7,050
	$ 10,502	$ 8,722

The servicing rights are amortized over 10 years, based on the maturity of the underlying mortgages.

During the year, goodwill increased by $1,384 related to the purchase of Canada ICI (note 10). In addition, goodwill increased by $585 related to the purchase of MTCL (note 16). The increases relate to payments required under contingent purchase price arrangements.

10. ACQUISITIONS

On February 28, 2002, MCLP completed the acquisition of the Canada ICI Mortgage Services Group (Canada ICI). These consolidated financial statements include the Company's 50% proportionate share of the following amounts. The allocation of the purchase price is summarized below:

	2003
Cost of acquisition paid in:	
Acquisition costs	$ –
Cash to vendors	2,768
	$ 2,768
Cost allocated to:	
Cash	$ –
Capital assets	–
Other assets	–
Liabilities	–
Goodwill	2,768
	$ 2,768

The purchase of Canada ICI was satisfied through an initial payment of $8.908. The Purchase and Sale Agreement includes contingent payments in cash and shares of the Company based on the operating results of the acquired business over three years following the acquisition date. In April 2003, a contingent payment in cash was required, based on the operating results for the 12 months ended February 2003. This has resulted in an increase of $2.768 to goodwill in MCLP and a proportionate increase of $1,384 in the Company's consolidated financial statements. If subsequent contingent payments are made, there will be further adjustments to the purchase price and goodwill.

Related to this acquisition, MCLP acquired commercial loan servicing rights for $1.835. The Company's proportionate share of these servicing rights is being amortized on a straight-line basis over 10 years, based on the maturity of the underlying mortgages.

11. LOANS RECEIVABLE

	2003	
Loan receivable from MCLP	$ 6,554	$ [illegible]
Accrued interest – loan receivable from MCLP	768	[illegible]
Loan receivable from MMC	546	[illegible]
Loan receivable from MSC	783	[illegible]
Loan receivable from Warehouse Trust	7,082	[illegible]
Accrued interest – loan receivable from Warehouse Trust	34	–
	$ 15,767	$ 8,452

The loan receivable from MCLP represents the portion of the loans receivable by the Company which is not eliminated when MCLP is proportionately consolidated in these consolidated financial statements. This loan receivable is due on demand and bears interest at 15.5% per annum. The loan receivable from MMC represents a stream of payments payable annually at $100 per annum with nine years remaining, purchased by the Company at a discount rate of 14.3%. The loan receivable from MSC is due one year plus a day after demand and bears interest at prime plus 1.5%, 6.0% at December 31, 2003 (2002 – 6.0%).

MFC acts as trustee of Warehouse Trust, a residential construction mortgage loan accumulation entity, which is beneficially owned by an unrelated financial institution. The loan receivable from Warehouse Trust relates to advances by the Company for mortgage fundings. The loan receivable bears interest at the rate of return earned by Warehouse Trust less 1.5%, and is repaid monthly. At December 31, 2003, this rate was 6.37%.

…ollar amounts in thousands except for per share amounts)

… ASSETS

	Note	2003	2002
Prepaid expenses		$ 428	$ 253
Deferred origination expenses		839	817
Deferred financing costs	15	2,677	2,880
Future tax assets	17	2,588	1,817
Deferred purchase price receivable	6	4,118	1,527
Recoverable program costs		1,068	–
		$ 11,718	$ 7,294

Recoverable program costs are to be recovered from Warehouse Trust over a seven-year period.

[illegible]

	2003	2002
Debentures	$ 262,190	$ 218,908
Accrued interest	5,256	3,711
	$ 267,446	$ 222,619
Fair market value	$ 270,084	$ 225,765

Debentures are issued to various individuals and institutions with original maturities ranging from 30 days to 5 years (2002 – 30 days to 5 years) and bear interest at rates ranging from 1.45% to 6.45% (2002 – 1.50% to 6.45%).

…NS PAYABLE

	2003	2002
(a) Royal Bank of Canada	$ 650	$ 602
(b) Bank of Montreal	-	6,333
(c) Bank of Montreal	-	5,000
	$ 650	$ 11,935

(a) The Royal Bank of Canada loan is an operating line and bank overdraft provided to MTCL. The line of credit is a demand-operating loan bearing interest at prime plus 0.85%, 5.35% at December 31, 2003 (2002 – 5.35%). The total facility available is $7,550. MTCL has provided a general security agreement covering all of its assets as collateral for the demand loan.

(b) The line of credit from Bank of Montreal includes a senior facility of $22,500 and a subordinated facility of $2,500. The program related to this facility is now closed and the loans have been repaid.

(c) The line of credit from Bank of Montreal is a $10,000 facility bearing interest at prime plus 0.5%. This facility is due and payable upon demand.

…DINATED DEBENTURE

On February 28, 2002, the Company arranged with Bentall Capital II Limited Partnership (BCLP) a $20,000 unsecured, subordinated debenture, convertible at any time by BCLP into 50.1% of the outstanding shares of MFC. The interest on the debenture is calculated at 15% per annum, payable monthly in arrears, and the principal is due at the end of the 15-year term. In addition, Cadim Inc. has agreed to provide up to $200,000 of credit enhancement facilities for use by MFC in its mortgage securitization programs.

Relating to this financing the Company incurred $3,050 of financing costs and the debenture was discounted $2,710. These costs are deferred and amortized on a straight-line basis over the 15-year term of the debenture.

16. SHARE CAPITAL

The authorized share capital of the Company is unlimited common shares with no par value.

Issued	#	2003	#	2002
Common shares	9,738,305	$ 56,770	9,615,906	$ 55[illegible]
Warrants	3,400,000	2,210	3,400,000	2,210
		$ 58,980		$ 57,40[illegible]

During 2003, the Company issued 122,399 shares for the quarterly dividends to shareholders in the dividend reinvestment plan.

During 2002, the Company issued 960,000 common shares at $7.50 per share to BCLP and 333,333 common shares at $8.25 per share to Crown Life. The Company also issued 3,400,000 warrants to BCLP at $0.65 per warrant. The warrants are exercisable until February 28, 2007 at an exercise price of $7.50 per share.

During 2001, the purchase of 90% of the outstanding shares of MTCL was satisfied through the issue of 593,602 common shares of the Company and cash payments of $357. Included in the total shares were 78,000 shares held in escrow. The value of these shares was deducted from the total purchase price. These shares have been released from escrow based on the earnings of MTCL to April 2003. The Company has recorded an increase of $7.50 per share to the purchase price and a corresponding increase in share capital and goodwill in 2003.

The details of share capital transactions for the two years ended December 31, 2003 are as follows:

	Common Shares		Warrants	
Issued	#	$	#	$
Balance as at January 1, 2002	[illegible]	46,32[illegible]		
Issued	[illegible]	[illegible]	[illegible]	[illegible]
Share issue costs		[illegible]		
Balance as at January 1, 2003	[illegible]	55[illegible]	3,400,0[illegible]	[illegible]
Issued	[illegible]	[illegible]		
Release of shares from escrow		[illegible]		
Balance as at December 31, 2003	**9,738,305**	**56,770**	**3,400,000**	**2,210**

Executive Stock Option Plan

During 2002, the Board of Directors (the "Board") established the Company's 2002 Executive Stock Option Plan (the "Stock Option Plan"). The aggregate number of common shares reserved for issuance under the Stock Option Plan is 416,129. The maximum number of common shares reserved for issuance under the Stock Option Plan is limited to 5% of the issued and outstanding common shares. There were no options issued during 2003 or 2002 and at December 31, 2003 and 2002 there were no options outstanding.

Executive Share Purchase Plan

During 2003, the Board established the Company's Executive Share Purchase Plan (the "Share Purchase Plan") whereby the Board can approve interest free loans to key personnel for the purpose of purchasing the Company's shares. The maximum amount of loans approved under the Share Purchase Plan is limited to 5% of the issued and outstanding common shares. The Company approved loans of $1,880 in 2003, however, at December 31, 2003, no loans were advanced under this plan. The loans under the Share Purchase Plan are interest free and have a five-year term.

2003 (Dollar amounts in thousands except for per share amounts)

INCOME TAXES

	2003	2002
Income before income taxes	$ 8,393	$ 5,734
Less dividends	(6,464)	(6,280)
Income subject to tax	1,929	(546)
Statutory rate of tax	37%	39%
Tax provision before the following:	714	(213)
Equity income	(302)	(375)
Change in valuation reserve	(182)	1,099
Provision for large corporations tax	178	160
Rate change on opening balance	228	-
Permanent differences	(490)	(367)
Tax provision per financial statements	$ 146	$ 304

The details of the future tax assets (liabilities) are as follows:

	2003	2002
Loss carryforward benefit	$ 3,506	$ 1,430
Provision for loan losses	798	850
Capital assets	(349)	(373)
Deferred (costs) revenue	(298)	1,225
Investment assets	(152)	(216)
Valuation reserve	(917)	(1,099)
	$ 2,588	$ 1,817

The Company is a Mortgage Investment Corporation under the Tax Act. As such, it is permitted to deduct from income for tax purposes dividends paid to shareholders during the year and within 90 days thereafter. The Company intends to continue conducting its affairs in such a manner as to continue qualifying as a Mortgage Investment Corporation under the Tax Act.

The Company has loss carryforward amounts of $9,475, which will expire as follows:

2008	$ 2,739
2010	$ 6,736

INTEREST RATE SENSITIVITY

Interest rate risk arises when principal and interest cash flows, both on and off balance sheet, including final maturities, have mismatched repricing dates. Interest rate risk, or sensitivity, is the potential impact of changes in interest rates on financial assets and liabilities.

An interest rate gap is a common measure of interest rate sensitivity. A positive gap occurs when more assets than liabilities reprice within a particular time period. A negative gap occurs when there is an excess of liabilities over assets repricing. The former provides a positive earnings impact in the event of an increase in interest rates during the time period. Conversely, negative gaps are positively positioned for decreases in interest rates during that particular time period. The determination of the interest rate sensitivity or gap position is based upon the earlier of the repricing or maturity date of assets, liabilities and includes numerous assumptions.

The gap position presented is measured at close of business on December 31, 2003. That position is subject to significant change in subsequent periods based on changes in customer preferences and in the application of asset/liability management policies.

Floating rate assets and liabilities are immediately sensitive to a change in interest rates while other assets are sensitive to changing interest rates periodically, either as they mature as interest payments are collected or paid, or as contractual repricing events occur. Non-interest rate sensitive assets and liabilities are not directly affected by changes in interest rates.

The following table presents the assets and liabilities of the Company by interest rate sensitivity:

	Floating Rate	Within 3 Months	3 Months to 1 Year	1 to 5 Years	Over 5 Years	Non-Interest Sensitive	2003 Total	2002 Total
Assets								
Investments								
Cash and cash equivalents	$ 6,122	$ [illegible]	$ [illegible]	–	$ –	$ –	**$ 31,395**	$ 9,4[illegible]
Mortgages	73,057	[illegible]	[illegible]	[illegible]	2,777	1,339	**240,937**	250,935
Other investments	10,106	[illegible]	[illegible]	[illegible]	–	12,046	**36,776**	31,65[illegible]
	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	**309,108**	292,02[illegible]
Accounts receivable	–	–		–	–	17,539	**17,539**	4,79[illegible]
Capital assets	–				–	4,843	**4,843**	5,77[illegible]
Goodwill and intangible assets	–			–	–	10,502	**10,502**	[illegible]
Loans receivable	7,865			–	7,100	802	**15,767**	[illegible]
Other assets	–			–	2,180	9,538	**11,718**	7,294
Total assets	$ 97,150	$ [illegible]	[illegible]	$ [illegible]	$ 12,057	$ 56,609	**$ 369,477**	[illegible]
Yield	5.7[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	–	**-**	[illegible]
Liabilities and Shareholders' Equity								
Debentures	$ [illegible]	[illegible]	[illegible]	[illegible]	$ –	$ –	**$ 267,446**	$ 222,61[illegible]
Accounts payable and accrued charges				–	–	22,019	**22,019**	[illegible]
Loans payable	[illegible]			–	–	–	**650**	[illegible]
Subordinated debenture		[illegible]		–	17,621	–	**17,621**	[illegible]
Shareholders' equity				–	–	61,741	**61,741**	[illegible]
Total Liabilities and Shareholders' Equity	$ [illegible]	[illegible]	[illegible]	[illegible]	$ 17,621	$ 83,760	**$ 369,477**	[illegible]
Yield	[illegible]	[illegible]	[illegible]	[illegible]	17.03%	–	**-**	
Gap	$ 96[illegible]	[illegible]	[illegible]	50,[illegible]	$ (5,564)	$ (27,151)	**$ -**	$ [illegible]
Off Balance Sheet Item								
Reverse repurchase obligations	23,[illegible]	[illegible]		–	–	–	**-**	
Net Position	$ 120,[illegible]	[illegible]	[illegible]	$ 50,292	$ (5,564)	$ (27,151)	**$ -**	$ -
Yield Spread	[illegible]	[illegible]	[illegible]	2.32%	(5.30)%	–	**-**	

r amounts in thousands except for per share amounts)

Fees from origination and administration services of the Company were:

Joint Venture Level

	2003	2002
MCLP		
Residential construction loan origination fees	$ 1,981	$ 2,588
Commercial loan origination fees	5,475	4,769
Construction and commercial loan servicing fees	9,642	8,501
Total MCLP fees	$ 17,098	$ 15,858
Consolidated Level		
Proportionately consolidated (50% of MCLP)	$ 8,549	$ 7,929
Partnership priority distribution	(857)	(833)
Construction loan origination and servicing fees	-	1,650
Leasing fees	2,039	1,899
Other fees	4,104	2,814
Consolidated fees	$ 13,835	$ 13,459

The Company participates in residential mortgage origination and administration through its equity investment in MSC and MMC.

MATION

The Company operates in three key business segments: investing operations, mortgage operations and leasing operations. Investing operations include asset/liability management, risk management, credit, and corporate banking. Mortgage operations generate fee and equity income from the origination, underwriting, funding, servicing and trading of single-family residential, residential construction and commercial mortgages. Leasing operations are in the Company's subsidiary MTCL, and generate income from originating, underwriting and funding as well as sales and servicing of equipment lease receivables.

Results of Business Segments – 2003

	Investing Operations	Mortgage Operations	Leasing Operations	Total
Investment income				
Interest income	$ 18,162	$ 982	$ -	$ 19,144
Leasing income	-	-	5,723	5,723
Other income	2,376	2,384	-	4,760
MSC equity income	-	817	-	817
	20,538	4,183	5,723	30,444
Financial expenses				
Interest expense	9,796	-	16	9,812
Other expenses	1,510	-	868	2,378
	11,306	-	884	12,190
Net investment income	9,232	4,183	4,839	18,254
Net fee income	1,156	8,192	2,039	11,387
Operating expenses	3,297	12,596	5,355	21,248
Income (loss) before income taxes	7,091	(221)	1,523	8,393
Income taxes and large corp. taxes	137	42	(33)	146
Net income (loss)	$ 6,954	$ (263)	$ 1,556	$ 8,247
Total assets	$ 320,446	$ 34,737	$ 14,294	$ 369,477
Amortization of capital assets	$ -	$ 1,223	$ 285	$ 1,508

Results of Business Segments – 2002

	Investing Operations	Mortgage Operations	Leasing Operations	Total
Investment income				
Interest income	$ [illegible]	$ 714	$ –	$ 14,272
Leasing income	–	–	6.001	6.001
Other income	[illegible]	2,341	–	5.304
MSC equity income	–	961	–	96
	[illegible]	[illegible]	[illegible]	[illegible]
Financial expenses				
Interest expense	[illegible]	–	[illegible]	[illegible]
Other expenses	[illegible]	–	1.281	3.554
	[illegible]		[illegible]	[illegible]
Net investment income	[illegible]	4,016	4.686	15.495
Net fee income	[illegible]	8,678	1.899	11.317
Operating expenses	[illegible]	[illegible]	[illegible]	[illegible]
Income before income taxes	[illegible]	[illegible]	[illegible]	[illegible]
Income taxes and large corp. taxes	[illegible]	[illegible]	[illegible]	[illegible]
Net income	[illegible]	$ [illegible]	$ [illegible]	$ [illegible]
Total assets	[illegible]	$ [illegible]	$ [illegible]	$ [illegible]
Amortization of capital assets		$ 1,560	$ 268	$ 1,828

21. EARNINGS PER S[illegible]

The following table sets forth the computation of basic and diluted earnings per share.

	2003	[illegible]
Numerator for basic and diluted earnings per share available to common shareholders	**$ 8,247**	$ 5,430
Denominator for basic earnings per share – Weighted average shares outstanding (000s)	**9,693**	9,40[illegible]
Effect of potentially dilutive securities: Warrants	**229**	354
Denominator for diluted earnings per share	**9,922**	9,761
Earnings per share		
Basic	**$ 0.85**	$ 0.58
Diluted	**$ 0.83**	$ 0.56

3 (Dollar amounts in thousands except for per share amounts)

ENTURE OPERATIONS

The Company has a 50% interest in MCLP, which is accounted for using the proportionate consolidation method.

A summary of the Company's proportionate interest in the joint venture at December 31, 2003 and 2002 is as follows:

Statement of Loss and Deficit

	2003	2002
Revenue from operations	$ 8,194	$ 7,786
Operating expenses	8,623	8,211
Priority distribution to other Partner	857	833
Net loss	$ (1,286)	$ (1,258)
Deficit, beginning of year	(2,606)	(560)
Distribution to Crown Life	-	(788)
Deficit, end of year	$ (3,892)	$ (2,606)

Balance Sheet

	2003	2002
Cash and cash equivalents	$ 785	$ 645
Goodwill and intangible assets	7,389	6,159
Other assets	4,476	2,874
	$ 12,650	$ 9,678
Accounts payable and accrued charges	$ 3,920	$ 3,533
Related party payables	5,455	2,592
Long-term debt	6,667	5,659
	16,042	11,784
Partners' capital	500	500
Partners' deficiency	(3,892)	(2,606)
	(3,392)	(2,106)
	$ 12,650	$ 9,678

Statement of Cash Flows

	2003	2002
Operating activities	$ 498	$ 2,979
Investing activities	(1,669)	(6,443)
Financing activities	1,311	3,981
Increase in cash and cash equivalents	140	517
Cash and cash equivalents, beginning of year	645	128
Cash and cash equivalents, end of year	$ 785	$ 645

AND CAPITAL RATIOS

The Company operates as a Mortgage Investment Corporation as defined under the Tax Act. Under the Tax Act, the Company's ability to accept deposits from the public is limited through the regulation of its borrowing ratio which is defined as the ratio of deposits and other borrowings to capital and reserves. The calculation of this ratio is determined on a non-consolidated basis and adjusted to cost for tax purposes. The maximum authorized borrowing ratio of the Company is currently 5.0. As at December 31, 2003 the ratio was 4.25 (2002 – 3.74).

The Company is a loan company regulated under the Trust and Loan Companies Act. The Trust and Loan Companies Act defines two tiers of capital and computes capital ratios in relation to risk-weighted assets. OSFI has issued guidelines to federally regulated companies for capital adequacy, which include meeting a minimum ratio of 8%. As at December 31, 2003, the ratio was 16.60% (2002 – 19.10%).

The second capital adequacy requirement of OSFI is an asset to capital multiple, which is calculated by dividing the Company's total consolidated regulatory assets by its total consolidated regulatory capital. The Company's required regulatory

capital ratio is a maximum multiple of 9. As at December 31, 2003, the Company has a regulatory assets to regulatory capital multiple of 8.89 (2002 – 6.96).

24. HEDGING INSTRUMENTS

At December 31, 2003, the Company had outstanding contracts to sell Government of Canada Bonds in the amount of $23,960 (2002 – $4,270). These contracts represent short positions, which are hedged against a portion of the Company's mortgages held for resale. The unrealized loss of these contracts was $68 (2002 – nil) at the year-end. The loss on these hedge contracts has been deferred, and will be recognized in income when the related hedged assets are sold.

25. COMMITMENTS AND CONTIN

The future minimum annual lease commitments for premises are as follows:

2004	$	3,794
2005		3,591
2006		3,594
2007		3,502
2008		2,993
Thereafter		15,975
	$	[illegible]

The Company has an unsecured letter of credit facility issued from the Bank of Montreal in the amount of $25,000. The facility is available by way of letter of credit with a term of up to one year from the date of issuance, plus a renewal clause providing for an automatic one-year extension at the maturity date subject to the Bank's option to cancel by written notice at least 30 days prior to the letters of credit expiry date.

The Company has a revolving letter of credit facility available from the Bank of Montreal in the amount of $5,000. The facility is for the purpose of issuing letters of credit to secure the performance and completion of obligations by residential building companies to municipalities. The facility requires the pledging of cash and/or Government of Canada Treasury Bills to secure the letters of credit issued.

26. ASSETS UNDER AD

Assets under administration consist primarily of leases and financial contracts as well as various construction and commercial loans and cash collateral accounts administered on behalf of investors. The Company earns origination and administration fees on these assets. Assets administered of $12,912,015 (2002 – $10,506,826) by MSC, the Company's affiliate, are not included below.

	2003	2002
Leases and financial contracts	$ 77,797	$ 74,550
Construction and commercial loans	4,545,273	4,309,930
Cash collateral and escrow	67,288	48,739
	$ 4,690,358	$ 4,433,219

27. RETIREMENT PROGRA

The Company has established retirement programs for its employees, including a group registered retirement savings plan (GRSP) and a deferred profit sharing plan (DPSP). The Company matches employee contributions to the GRSP to the following levels after one year of service. The maximum Company contributions are $7.25 per employee.

Years of Service	Percentage of Employee Earnings
1–5	2.5
6–10	5.0
11 and over	7.5

llar amounts in thousands except for per share amounts)

The Company makes additional contributions to the DPSP account of individuals who have been employed by the Company as at December 31, 1998 as follows:

Year of Service to MCAP and/or Clarica Life prior to December 31, 1998	Percentage of Employee Earnings
0–2	0.5
3–5	0.75 to 3.75
6–10	1.0 to 4.0
11 and over	1.25 to 4.25

The level of DPSP contribution also depends on the age of the employee at December 31, 1998.

The retirement program expenses recorded for the year ended December 31, 2003 were $253 (2002 – $275).

ARE OWNERSHIP PROGRAM

The Company has established a share ownership program for its employees. The plan provides employees the opportunity to purchase shares of MCAP Inc. The Company matches employee purchases to the following levels:

Participating employees may purchase no less than 1% and up to a maximum of 6% of their annual base salary. The Company will match 50% of the purchase price, up to a maximum of 3% of the employee's annual base salary. The Company's contributions remain unvested until December 31st of the year they were purchased.

The employee share ownership program expenses recorded for the year ended December 31, 2003 were $83 (2002 – $92).

ATIVE AMOUNTS

Certain comparative amounts have been reclassified to conform to the presentation adopted in the current year.

REORGANIZATION

On December 10, 2003, CDP Capital – Real Estate Advisory Inc. ("CDP Capital – Real Estate Advisory"), a subsidiary of the Caisse de dépôt et placement du Québec ("Caisse"), and the Company announced they have entered into a non-binding memorandum of understanding regarding the merger of the activities of MFC, with the origination and servicing activities of CDP Capital – Mortgages, a member of the Caisse, by combining the operations and restructuring MCAP Commercial Limited Partnership which will operate as MCAP Capital Limited Partnership. Completion of the transaction is subject to numerous conditions, including satisfactory due diligence, Board of Director approval, regulatory and shareholder approvals (if any), and completion of definitive documentation. Subject to satisfactory completion of these conditions, the transaction is scheduled to close in the first half of 2004. There were no agreements signed or executed at the date of release of these consolidated financial statements.

In the ordinary course of business, the Company is subject to legal claims. Such claims generally arise in the Company's role as agent and nominee and are ultimately settled with third-party investors or borrowers. Management has assessed claims and possible claims as of the year-end and believes any unaccrued claims would not have a material adverse effect on the Company.

Subsequent to year-end, the Company settled an amount of $7,500 relating to two guarantees provided by Interior Capital Corporation (ICC). The Company acquired ICC on January 1, 2000 as part of a merger transaction. The merger transaction documents provided that the vendor shareholders of ICC would pay all costs incurred by the Company pursuant to the representations and warranties made by the vendor shareholders at the time of the merger. Pursuant to the merger transaction documents, the Company has signed agreements with the vendor shareholders of ICC to recover the costs related to the settlement of these guarantees. The Company received concurrently with the settlement $3,511 of the recovery from the vendor shareholders of ICC and the remainder will be received over five years. Interest is being charged on the unpaid amounts at market rates of 4.0%. The vendor shareholders of ICC are related to the Company. As a result of these transactions, the amount of $7,500 is included in both Accounts receivable and Accounts payable and accrued charges. There is no change to net income or shareholders' equity as a result of this matter.

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(Dollars in thousands except for pe

Year Ended December 31,	2003	2002	2001
Investment Income			
Mortgage interest income	$ 17,162	$ 12,990	$ 15,303
Interest on cash and cash equivalents	1,982	1,282	2,042
Leasing income	5,723	6,001	2,204
Other income	5,577	6,265	5,643
	30,444	26,538	25,192
Financial Expenses			
Interest expense	9,812	7,489	10,212
Other expenses	2,378	3,554	2,015
	12,190	11,043	12,227
Net investment income	18,254	15,495	12,965
Fee income	13,835	13,459	13,720
Related interest and fees	(2,448)	(2,142	
Net fee income	11,387	11,317	13,720
Revenue from operations	29,641	26,812	26,685
Operating Expenses			
Salaries and administrative	17,072	17,024	16,885
Occupancy	1,573	1,795	1,920
Information systems	2,603	2,259	1,104
	21,248	21,078	19,909
Income before income taxes	8,393	5,734	6,776
Provision for (recovery of) income taxes and large corporation taxes	146	304	(19)
Net income	$ 8,247	$ 5,430	$ 6,795
Earnings per share – basic	$ 0.85	$ 0.58	$ 0.85
Earnings per share – diluted	$ 0.83	$ 0.56	$ 0.85
Dividends per share	$ 0.68	$ 0.68	$ 0.68
Weighted average share # (000's)	9,693	9,407	7,978
Weighted average diluted share # (000's)	9,922	9,761	7,978
Total assets	$ 369,477	$ 327,059	$ 222,397
Total liabilities	$ 307,736	$ 268,676	$ 174,248
Consolidated assets under administration	$ 4,690,358	$ 4,433,219	$ 3,753,491
Group assets under administration	$ 17,602,373	$ 14,940,045	$ 11,551,934

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Income Statement				2003				2002
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Investment income								
Mortgage interest income	$ 4,057	$ 4,355	$ 4,134	$ 4,616	$ 3,690	$ 3,862	$ 2,930	$ 2,508
Interest on cash and cash equivalents	672	486	466	358	502	357	216	207
Leasing income	1,735	1,148	1,556	1,284	1,961	1,414	1,377	1,249
Other income	797	1,491	1,626	1,663	2,403	1,489	1,289	1,084
	7,261	**7,480**	**7,782**	**7,921**	**8,556**	**7,122**	**5,812**	**5,048**
Financial expenses								
Interest expense	2,433	2,505	2,467	2,407	2,053	1,980	1,855	1,601
Other expenses	621	587	470	700	1,254	670	893	737
	3,054	**3,092**	**2,937**	**3,107**	**3,307**	**2,650**	**2,748**	**2,338**
Net investment income	4,207	4,388	4,845	4,814	5,249	4,472	3,064	2,710
Fee income	4,067	3,427	3,070	3,271	3,245	3,143	2,969	4,102
Related interest and fees	(562)	(612)	(628)	(646)	(647)	(663)	(624)	(208)
Net fee income	3,505	2,815	2,442	2,625	2,598	2,480	2,345	3,894
Revenue from operations	7,712	7,203	7,287	7,439	7,847	6,952	5,409	6,604
Operating expenses								
Salaries and administrative	4,376	4,275	4,166	4,255	4,811	4,072	4,007	4,134
Occupancy	401	367	392	413	548	558	401	288
Information systems	589	649	645	720	532	519	597	611
	5,366	**5,291**	**5,203**	**5,388**	**5,891**	**5,149**	**5,005**	**5,033**
Income before income taxes	2,346	1,912	2,084	2,051	1,956	1,803	404	1,571
Provision for (recovery of) income taxes and large corporation taxes	47	(48)	99	48	(23)	124	41	162
Net income for the period	**$ 2,299**	**$ 1,960**	**$ 1,985**	**$ 2,003**	**$ 1,979**	**$ 1,679**	**$ 363**	**$ 1,409**
Earnings per share	**$ 0.24**	**$ 0.20**	**$ 0.20**	**$ 0.21**	**$ 0.21**	**$ 0.17**	**$ 0.04**	**$ 0.16**
Diluted earnings per share	**$ 0.23**	**$ 0.20**	**$ 0.20**	**$ 0.20**	**$ 0.20**	**$ 0.17**	**$ 0.04**	**$ 0.16**
Dividends per share	**$ 0.17**	**$ 0.17**	**$ 0.17**	**$ 0.17**	**$ 0.17**	**$ 0.17**	**$ 0.17**	**$ 0.17**
Weighted average # of shares (000's)	**9,738**	**9,693**	**9,678**	**9,645**	**9,616**	**9,616**	**9,616**	**8,768**
Weighted average # of diluted shares (000's)	**10,029**	**9,867**	**9,819**	**9,926**	**9,986**	**10,038**	**10,070**	**8,850**

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(Dollars in thousands except for per shar

Balance Sheet (000's)				**2003**				2002
	Q4	**Q3**	**Q2**	**Q1**	Q4	Q3	Q2	Q1
Assets								
Investments								
Cash and cash equivalents	$ 31,395	$ 14,372	$ 34,529	$ 43,319	[illegible]	$ 4,944	$ 31,955	$ 5,064
Mortgages	240,937	274,487	237,967	257,289	[illegible]	217,380	202,048	178,084
Other investments	36,776	29,981	29,411	26,817	[illegible]	[illegible]	[illegible]	[illegible]
	309,108	**318,840**	**301,907**	**327,425**	[illegible]	[illegible]	**263,596**	**206,875**
Accounts receivable	17,539	11,690	7,389	7,211	[illegible]	[illegible]	[illegible]	[illegible]
Capital assets	4,843	5,144	5,360	5,659	[illegible]	[illegible]	[illegible]	[illegible]
Goodwill and intangible assets	10,502	10,550	10,597	10,059	8,722	8,723	8,726	8,634
Loans receivable	15,767	17,497	9,670	8,367	[illegible]	7,066	6,883	[illegible]
Other assets	11,718	8,152	7,301	7,409	[illegible]	[illegible]	[illegible]	[illegible]
	$ 369,477	**$ 371,873**	**$ 342,224**	**$ 366,130**	[illegible]	**$ 286,841**	**$ 295,195**	**$ 239,173**
Liabilities and Shareholders' Equity								
Liabilities								
Debentures	$ 267,446	$ 280,244	$ 252,417	$ 274,896	[illegible]	$ 195,459	$ 202,213	[illegible]
Accounts payable and accrued charges	22,019	12,738	11,119	14,750	[illegible]	9,376	7,885	9,014
Loans payable	650	218	738	–	11,935	6,612	9,792	6,289
Subordinated debenture	17,621	17,576	17,531	17,486	17,441	17,395	17,350	17,305
	307,736	**310,776**	**281,805**	**307,132**	[illegible]	**228,842**	**237,240**	**179,946**
Shareholders' equity								
Share capital	58,980	58,980	58,738	57,657	57,405	57,405	57,405	57,405
Retained earnings	2,761	2,117	1,681	1,341	978	594	550	[illegible]
	61,741	**61,097**	**60,419**	**58,998**	**58,383**	**57,999**	**57,955**	**59,227**
	$ 369,477	**$ 371,873**	**$ 342,224**	**$ 366,130**	[illegible]	[illegible]	[illegible]	[illegible]

of MCAP Inc.

Margaret Barrett, M.A.
CEO, North America Merryck & Co.
Member of the Human Resources and Compensation Committee; Chairman of the Conduct Review and Corporate Governance Committee;
Director since February 2000

David Broadhurst, B.A., C.A.
President, Poynton Investments Limited; Member of the Conduct Review and Corporate Governance Committee;
Chairman of the Audit Committee;
Director since May 1997

André Collin
President and COO,
CDP Capital – Real Estate Advisory Inc.; Member of the Investment Committee;
Member of the Human Resources and Compensation Committee;
Director since February 2002

Raymond Doré, C.A.
Chairman, MCAP Inc. and MCAP Financial Corporation;
Director since May 1997

Brian Johnson, B.COM., M.B.A., F.L.M.I., C.F.A.
President and CEO,
Crown Life Insurance Company;
Member of the Investment Committee; Chairman of the Human Resources and Compensation Committee;
Director since January 2001

David MacIntosh, M.A.
Corporate Director; Chairman of the Investment Committee;
Member of the Audit Committee;
Director since January 2000

Derek Norton, B.COM.
President and CEO, MCAP Inc.;
Director since July 2000

Ian Sutherland, B.COM., C.A., C.F.A.
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Director since January 1991

James Wright, M.B.A., J.D.
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Member of Audit Committee;
Member of Conduct Review and Corporate Governance Committee;
Director since May 2002

management, MCAP Inc.

Raymond Doré
Chairman

Derek Norton
President and CEO

Blaine Welch
Senior Vice-President and Chief Risk and Investment Officer

Lorne Jenkins
Vice-President and CFO

Anthony Stilo
Chief Audit Officer

Kenneth Teskey
Chief Compliance Officer and Corporate Secretary

of the MCAP Group of Companies

Raymond Doré
Chairman, MCAP Inc. and MCAP Financial Corporation

Derek Norton
President and CEO, MCAP Inc.;
CEO, MCAP Financial Corporation and MCAP Service Corporation

Blaine Welch
Senior Vice-President and Chief Risk and Investment Officer, MCAP Inc.; Senior Vice-President, MCAP Financial Corporation

Lorne Jenkins
Vice-President and CFO, MCAP Inc. and MCAP Financial Corporation

Philip Asseff
President and CEO, MCAP Securities Inc.

Eugene Basolini
President and COO, MTC Leasing Inc.

Scott Cameron
President, MCAP Equity Advisors

Dale Klein
President and CEO, Canada ICI Commercial Mortgages Inc.

Steven Maker
President and COO,
MCAP Financial Corporation and MCAP Service Corporation;
COO, MCAP Mortgage Corporation

Ronald Swift
President and CEO, MCAP Mortgage Corporation

Robert Stuebing
Senior Vice-President, Investment Banking, MCAP Financial Corporation

Alric McGratten
Executive Vice-President, MCAP Financial Corporation

CORPORATE

Mark Aldridge
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Vice-President, Human Resources

Gordon Herridge
Vice-President and CFO,
MCAP Service Corporation,
MCAP Mortgage Corporation and CFO and Corporate Secretary, MTC Leasing Inc.

Steve Holman
Vice-President, Corporate Planning and Analysis

Bruno Iacovetta
Vice-President, Capital Management

Claus Kretschmann
Vice-President, Enterprise Risk Management

Domenic Maggio
Vice-President, Infrastructure

Robert May
Vice-President, Technology Architecture

Tammy Oldenburg
CFO, MCAP Securities Inc. and Controller, MCAP Inc.

Carol Schutzman
Vice-President, Operational Excellence

Jack Shapiro
Vice-President, Marketing and Communications

Patti Somers
Vice-President and Chief Technology Officer

Anthony Stilo
Chief Audit Officer, MCAP Inc. and MCAP Financial Corporation

Kenneth Teskey
Chief Compliance Officer and Corporate Secretary, MCAP Inc. and MCAP Financial Corporation

John Thompson
Vice-President, Product Development, MCAP Service Corporation

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Robert Balfour
Vice-President, Real Estate Lending

Gerard Caverson
Vice-President, Real Estate Lending

Alexander Fox
Vice-President, Real Estate Lending

Robert Maciver
Vice-President, Real Estate Lending

Mark Yhap
President, Real Estate Lending

COMMERCIAL ORIGINATION

Fred Harris
Vice-President

Jim Leitch
Vice-President

Phil Lovera
Vice-President

Thomas Marcantonio
Vice-President

Peter Morrish
Vice-President

Bruce Roy
Vice-President

COMMERCIAL AND CONSTRUCTION SERVICING

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Senior Vice-President, Commercial Mortgages

RESIDENTIAL ORIGINATION AND SERVICING

Jeffery Armstrong
Vice-President, Residential Credit

Bryan Devries
Vice-President, Broker Lending

Cheryl Preston
Vice-President, National Servicing

Joe Santos
Regional Vice-President, Western Canada

Dan Wowk
Vice-President, Business Solutions

ASSET/PORTFOLIO MANAGEMENT

Nuala Taylor
Vice-President and Director

LEASING

Dara Coulter
Vice-President, Finance

Susan Cousineau
Vice-President, Operations

Ed Dias
Vice-President, Credit and Business Services

corporate directory and information

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200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

MCAP Financial Corporation

Toronto
200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

Vancouver
1140 West Pender Street
Suite 1400, V6E 4G1
604-681-8805 or 1-800-977-5877

Calgary
435 – 4th Avenue S. W.
Suite 250, T2P 3A8
403-266-5722

Halifax
2000 Barrington Street
Suite 522, B3J 3K1
902-422-1920

MCAP Mortgage Corporation

Toronto
200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

Vancouver
1140 West Pender Street
Suite 1400, V6E 4G1
604-681-8805 or 1-800-977-5877

Calgary
435 – 4th Avenue S. W.
Suite 250, T2P 3A8
403-266-5722

Kitchener
101 Frederick Street
Suite 200, N2H 6R2
519-743-8773 or 1-800-265-2624

MCAP Service Corporation

Toronto
200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

Edmonton
10235 – 101st Street
Suite 1312, T5J 3J8
780-414-0911 or 1-800-265-2624

Montreal
1550 Metcalfe Street
Suite 1510, H3A 1X6
514-282-8038 or 1-888-811-2529

Kitchener
101 Frederick Street
Suite 200, N2H 6R2
519-743-8773 or 1-800-265-2624

MCAP Securities Inc.

Toronto
200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

Montreal
1 Westmount Square
Suite 1250, H3Z 2P9
514-989-1909

MCAP Commercial LP

Toronto
200 King Street West
Suite 400, M5H 3T4
416-598-2665 or 1-800-387-4405

Regina
2221 Cornwall Street
Suite 400, S4P 4M2
306-546-6144 or 1-866-881-5580

Canada ICI Commercial Mortgages Inc.

*Victoria**
1110 Government Street
Suite 204, V8W 1Y2
250-380-7577
**correspondent office*

Vancouver
1050-1040 West Georgia Street
V6E 4H1
604-684-6700

Calgary
720-630 6th Avenue S. W.
T2P 0S8
403-297-9320

Edmonton
10060 Jasper Avenue
Suite 1750, T5J 3R8
780-990-1144

Toronto
36 Toronto Street
Suite 720, M5C 2C5
416-368-8844

Montreal
1010 Sherbrooke St. W.
Suite 405, H3A 2R7
514-499-8559

MTC Leasing Inc.

Burlington
3310 South Service Road
L7N 3M6
905-639-3995 or 1-800-263-5137

corporate information

AUDITORS

Ernst & Young LLP
Toronto, Ontario

BANK

Bank of Montreal
First Canadian Place
Toronto, Ontario

CORPORATE COUNSEL

Blake, Cassels & Graydon LLP
Toronto, Ontario

CORPORATE INFORMATION

This MCAP Inc. 2003 Annual Report is available for viewing/printing on our corporate web site at www.mcap.com. To request a printed copy, please contact Marketing and Communications, 200 King Street West, Suite 400, Toronto, ON M5H 3T4, by phone 416-598-2665 or 1-800-387-4405, or email mac@mcap.com (On peut obtenir sur demande un exemplaire en français.)

GENERAL INFORMATION

For general enquiries about Company news and initiatives, please contact Marketing and Communications. MCAP Inc.'s news releases are available on our corporate web site at www.mcap.com.

RATINGS BY STANDARD & POOR'S

Residential
Prime Servicer – Above Average
Subprime Servicer – Above Average

Commercial
Primary Servicer – Above Average
Special Servicer – Average
Master Servicer – Average

REGISTRAR AND TRANSFER AGENT

For dividend information, change in share registration or address, lost certificates, estate transfers, or to advise of duplicate mailings, please call MCAP Inc.'s Transfer Agent and Registrar at 1-800-332-0095, or write to Computershare Trust Company of Canada, 100 University Avenue, 9th Floor, Toronto, Ontario M5J 2Y1

WEB SITES

Corporate
mcap.com

Immigrant Investor
newcanadianplan.com

Investor Services
investorinquiry.com

Broker Lending
mcapbroker.com

Residential Mortgages
mcapmortgage.com

Commercial Mortgages
canadaici.com

Business Solutions
mcapdirect.com

For solicitors
mcapsolicitor.com

Leasing
mtcleasing.com

PUBLIC LISTING

Toronto Stock Exchange
Exchange symbol MKP

ANNUAL MEETING

May 6, 2004 at 4:00 p.m.
St. Andrew's Club and
Conference Centre
150 King Street West, 27th Floor
Toronto, Ontario

affiliations

MCAP is a member of the following organizations:
Alberta Mortgage Brokers Association
Canadian Banking Ombudsman
Canadian Finance and Leasing Association
Canadian Institute of Mortgage Brokers and Lenders
Canadian Investor Protection Fund
Canadian Management Centre
Commercial Mortgage and Lender Association
Investment Dealers Association
Mortgage Bankers Association of America
Mortgage Brokers Association of British Columbia
National Association of Industrial and Office Properties
Ontario Long Term Care Association
Urban Development Institute

MCAP is regulated by the following regulatory bodies:
Canada Deposit Insurance Corporation
Commercial Mortgage Securities Association (US)
Financial Consumer Agency of Canada
Financial Services Commission of Ontario
Financial Transactions & Reports Analysis Centre of Canada
Office of the Superintendant of Financial Institutions
Real Estate Institute of British Columbia
The Mortgage Loans Association of Alberta

MCAP receives mortgage insurance coverage from:
Canada Mortgage and Housing Corporation
GE Capital Mortgage Insurance Corporation

MCAP supports the following charitable organizations:
Habitat for Humanity
United Way

Design_Ove Design & Communications Ltd. Principal Photography_David Graham White Printing_Commerce Press

MCAP INC.

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